TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, [redacted] 1950

No. [redacted]310

GULF OIL CORPORATION, PETITIONER,

vs.

O. G. LEWELLYN, COLLECTOR OF INTERNAL REVENUE FOR THE FOURTH/THIRD DISTRICT OF PENNSYLVANIA

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT FILED

(26,248)

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1917.

No. 781.

GULF OIL CORPORATION, PETITIONER,

vs.

C. G. LEWELLYN, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

INDEX.

	Original.	Print
Caption	1	1
Transcript of record from the District Court of the United States for the Western District of Pennsylvania	4	2
Appearances	4	2
Docket entries	5	2
Præcipe for summons	7	3
State of claim	7	3
Exhibit A—Demand to remit assessment	14	7
B—Protest letter, Gulf Oil Corporation to Lewellyn, collector, &c., February 16, 1915	21	10
C—Claim under series 7, No. 14, revised, and series 7, No. 27, supplement No. 1, for taxes improperly paid, &c	22	11
D—Letter, Lewellyn, collector, &c., to Gulf Oil Corporation, April 13, 1915	29	14

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., MARCH 14, 1918.

	Original.	Print
Affidavit of defense	31	15
Præcipe for trial list	34	17
Stipulation waiving jury trial	34	17
Trial memorandum	35	17
Admissions of fact	36	18
Testimony of Walter J. Guthrie	42	20
Reporter's certificate	60	30
Judge's certificate	60	30
Request for findings of fact and conclusion of law	61	31
Opinion, Orr, J.	70	35
Order and exception	87	44
Judgment	88	44
Assignments of error	88	44
Petition for writ of error	92	46
Order allowing writ of error	92	47
Bill of exceptions	93	47
Judge's certificate	94	47
Clerk's certificate	95	48
Order of argument and submission	96	48
Opinion, McPherson, C. J.	97	49
Judgment	108	57
Clerk's certificate	109	58
Writ of certiorari and return	112	59
Exhibit		

1-2 Orig'l.

In the United States Circuit Court of Appeals for the Third Circuit, March Term, 1917.

No. 2254.

C. G. LEWELLYN, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, Plaintiff-in-Error,

vs.

GULF OIL CORPORATION, a Corporation Organized and Existing under the Laws of the State of New Jersey, Defendant-in-Error.

TRANSCRIPT OF RECORD.

E. Lowry Humes, United States Attorney; B. B. McGinnis, Special Assistant United States Attorney, Attorneys for Plaintiff-in-Error.
Reed, Smith, Shaw & Beal, Attorneys for Defendant-in-Error.

3 In the United States Circuit Court of Appeals for the Third Circuit, March Term, 1917.

No. 2254.

C. G. LEWELLYN, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, Plaintiff-in-Error,

vs.

GULF OIL CORPORATION, a Corporation Organized and Existing under the Laws of the State of New Jersey, Defendant-in-Error.

In Error to the District Court of the United States for the Western District of Pennsylvania.

Transcript of Record.

4 In the District Court of the United States for the Western District of Pennsylvania, May Term, 1916.

No. 1592.

GULF OIL CORPORATION, a Corporation Organized and Existing under the Laws of the State of New Jersey,

vs.

C. G. LEWELLYN, Collector of Internal Revenue for the Twenty-third District of Pennsylvania.

Appearances:

Reed, Smith, Shaw & Beal, Pittsburgh, Pa., Attorneys for Plaintiff.
E. Lowry Humes, United States Attorney and Attorney for Defendant.
B. B. McGinnis, Special Assistant United States Attorney and Attorney for Defendant.

Among the rolls, records and judicial proceedings had in the District Court of the United States, at No. 1592 May Term, 1916, may be found the following words and figures, to-wit:

5 *Docket Entries.*

February 15, 1916. Præcipe for summons and Plaintiff's Statement filed.
February 15, 1916. Summons in assumpsit issued ret'ble to first Monday of March next.
February 15, 1916. Writ returned served on C. G. Lewellyn, Collector of Internal Revenue by handing to and leaving a true and attested copy thereof with C. G. Lewellyn, Collector of Internal Revenue at Pittsburgh, Pa., February 15, 1916.
March 15, 1916. Affidavit of Defense filed.
April 1, 1916. Præcipe for trial list filed.
June 1, 1916. Continued to November Term, 1916.
August 22, 1916. Præcipe for trial list filed.
January 16, 1917. Stipulation waiving jury trial filed.
January 30, 1917. Trial (without a jury) begun.
January 30, 1917. Plaintiff's witness, Walter J. Guthrie, sworn.
January 30, 1917. Memoranda of trial filed.
January 30, 1917. Case argued, C. A. V.
January 30, 1917. Plaintiff's Request for Findings of Fact and Conclusions of Law, filed.
March 12, 1917. Order entered on Argument List; "And now, March 12th, 1917, Judgment directed to be entered in favor of the Plaintiff in the sum of $114,244.40 with interest from Febebruary 17, 1915. Per Curiam."

6 March 12, 1917. Opinion filed and entered.

March 17, 1917. Order filed and entered directing the clerk to enter judgment in sum of $128,524.95, etc., and noting exception to defendant.

March 17, 1917. Pursuant to Order of Court, judgment is hereby entered in favor of Gulf Oil Corporation and against C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, in the sum of One Hundred Twenty-eight Thousand, five hundred and twenty-four and 95-100 ($128,524.95) Dollars.

J. WOOD CLARK, *Clerk.*

April 14, 1917. Petition for Writ of Error and Order allowing same, filed and entered.

April 14, 1917. Assignments of Error filed.

April 16, 1917. Writ of Error allowed and issued.

April 16, 1917. Citation awarded and issued.

April 23, 1917. Bill of exceptions signed and sealed and filed.

April 23, 1917. Service of Citation accepted by Reed, Smith, Shaw & Beal.

7 *Præcipe and Statement of Claim.*

Filed February 15, 1916.

To J. Wood Clark, Esq., Clerk:

Issue summons in assumpsit in the above entitled case, returnable to next return day.

REED, SMITH, SHAW & BEAL,
Attorneys for Plaintiff.

February 15th, 1916.

Statement of Claim.

The Gulf Oil Corporation, plaintiff above named, brings this suit against C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, defendant above named, to recover the sum of $114,244.40, with interest from February 17, 1915, upon a cause of action whereof the following is a statement:

First. The Gulf Oil Corporation is a corporation duly organized under the laws of the State of New Jersey. C. G. Lewellyn is the Collector of Internal Revenue for the Twenty-third District of Pennsylvania, being duly commissioned as such pursuant to the laws of the United States of America.

8 Second. The Gulf Oil Corporation, on the 14th day of February, 1914, in compliance with the provisions of the Act of Congress of October 3, 1913, made a return of its annual net income for the twelve months ending December 31, 1913, as required by said Act. In making said return, the Gulf Oil Corporation certified that it had not included in the statement of gross in-

come for the year 1913 certain dividends amounting to $11,424,000.00 received by it from subsidiary companies out of earnings and surplus of said subsidiary companies accrued prior to January 1, 1913.

Third. In said return, the Gulf Oil Corporation showed net income for the twelve months ending December 31, 1913, of $886,250.44, but under date of May 1, 1914, the said C. G. Lewellyn, Collector, mailed to said corporation notice of an assessment of tax thereon amounting to $9,072.56. A claim for abatement of this overcharge, amounting to $210.06, was filed with the Collector June 9, 1914, and on June 30, 1914, the Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, the sum of $8,862.50, being the amount of said assessment, less the $210.06 for which abatement was claimed. Said claim for abatement having been disallowed, said Gulf Oil Corporation, on the 5th day of November, 1914, paid the said Collector the additional sum of $210.06, with interest amounting to $6.30, making a total payment of $216.36.

Fourth. On the 30th day of December, 1914, the said C. G. Lewellyn, Collector, acting under instructions from the Commissioner of Internal Revenue at Washington, D. C., mailed notice and demand for tax assessment against the Gulf Oil Corporation for the year ending December 31, 1913, amounting to $114,034.34. In fact, this additional assessment amounted to $114.244.40,
9 being the 1 per cent upon the entire amount of the dividends received by the Gulf Oil Corporation from subsidiary companies out of surplus accrued to such subsidiaries prior to January 1, 1913, and payable to the Gulf Oil Corporation prior to March 1, 1913, and said additional assessment was based solely on said dividends. In making the assessment, however, the Commissioner of Internal Revenue reconsidered and allowed the previous claim for abatement of $210.06, erroneously assessed against the corporation in the original assessment, and credited the same as having been paid upon the assessment of December 30, 1914, leaving the net balance of such assessment $114,034.34 as stated.

Fifth. The notice and demand of the said C. G. Lewellyn, Collector, for the payment of this additional tax recites that if the tax is not paid on or before January 8, 1915, it would be the duty of the Collector to collect said tax, together with 5 per cent additional and interest at the rate of 1 per cent per month until paid.

Sixth. That subsequently the plaintiff filed with the defendant for presentation to the Commissioner of Internal Revenue a claim for the abatement of said income tax amounting to $114,034.34, a copy of which claim is attached hereto and made a part hereof and marked "Exhibit A." That after an examination of said claim for abatement, the Commissioner of Internal Revenue rejected the same.

Seventh. On February 17, 1915, the said Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, said additional income tax as assessed for the period ending December 31, 1913, in
10 the sum of $114,034.34, and at the same time filed with said C. G. Lewellyn a written protest, a copy of which protest is attached hereto and made a part hereof and marked "Exhibit B."

Eighth. That subsequently the plaintiff filed with the said C. G. Lewellyn for presentation to the Commissioner of Internal Revenue, a claim for the refund of the net amount of the assessment of said income tax, to-wit: $114,034.34, and also the amount of the credit allowed thereon of $210.06, representing an over assessment against the corporation on the basis of its return as originally filed, the two amounts constituting the entire amount of the additional assessment in the sum of $114,244.40. A copy of the said claim for refund is hereto attached and made a part hereof and marked "Exhibit C."

Ninth. That after consideration of said claim for refund, the Commissioner of Internal Revenue rejected the same, and the said C. G. Lewellyn was instructed to notify the Gulf Oil Corporation, and on or about April 13, 1915, did so notify said corporation, that said claim was rejected, a copy of which notice is attached hereto and made a part hereof and marked "Exhibit D."

Tenth. The plaintiff avers that it is a holding company and that for many years prior to January 1, 1913, it has been the owner of all of the capital stock of the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company, the Gulf Pipe Line Company of Oklahoma, the Indiana Oil and Gas Company and the Gulf Commissary Company, except directors' qualifying shares, and was the owner of said shares during all of the period during which the earnings were accumulated out of which the dividends in question were declared. That
11 with the exception of the Indiana Oil and Gas Company and the Gulf Commissary Company, no dividends were paid by any of the above named subsidiary companies prior to December 31, 1912, but that all of the earnings of said companies were either invested, as earned, in the expansion and development of the companies mentioned, or were allowed to accumulate in their treasuries. In January, of 1913, the officers of the Gulf Oil Corporation, plaintiff, decided that the accumulated earnings and surpluses of these subsidiary companies should be taken over by the plaintiff company in the form of dividends, and accordingly:

Eleventh. On February 7, 1913, the J. M. Guffey Petroleum Company declared and authorized, out of its accumulated surplus, earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $3,749,750.00.

Twelfth. On February 7, 1913, the Gulf Pipe Line Company declared and authorized, out of its accumulated surplus, earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $4,724,055.00.

Thirteenth. On February 7, 1913, the Gulf Pipe Line Company of Oklahoma declared and authorized, out of its accumulated surplus, earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $2,597,660.00.

Fourteenth. On January 8, 1913, the Indiana Oil and Gas Company declared and authorized, out of its accumulated surplus,
12 earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received

$338,000.00; and on February 24, 1913, declared and authorized the immediate payment of a dividend, of which the Gulf Oil Corporation received $10,000.00.

Fifteenth. On December 17, 1912, the Gulf Commissary Company declared and authorized, out of its accumulated surplus, earned prior to December 17, 1912, the payment of a dividend, of which the Gulf Oil Corporation received $4,975.00.

Sixteenth. That the said J. M. Guffey Petroleum Company, Gulf Pipe Line Company, Gulf Pipe Line Company of Oklahoma, Indiana Oil and Gas Company and Gulf Commissary Company were all corporations, subject to the payment of the Excise Tax imposed by the Act of Congress of August 5, 1909, and that all of said companies had in fact paid all of the taxes imposed upon them under the provisions of the said Act, including such taxes on the earnings from which said dividends were declared.

Seventeenth. Plaintiff is advised and believes, and therefore avers, that there existed no warrant in law for the assessment, by the said Commissioner of Internal Revenue, of an additional Corporation Income Tax against the Gulf Oil Corporation for the period ending December 31, 1913, upon dividends received by it from subsidiary companies out of surplus earned and accumulated prior to January 1, 1913, and declared and payable to the Corporation prior to March 1, 1913; that there existed no warrant in law for the assessment of an additional Income Tax against the Gulf Oil Corporation,
13 herein complained of, under the provisions of the Act of October 3, 1913; that there existed no warrant in law for demanding and collecting from the Gulf Oil Corporation by the defendant, an additional Corporation Income Tax of $114,244.40, upon the additional assessment above referred to; and that there existed no warrant in law for the refusal by the said Commissioner of Internal Revenue to refund said tax of $114,244.40, consisting of the credit of $210.06, and the actual payment of February 17, 1915, of $114,034.34.

Eighteenth. That the assessment by the Commissioner of Internal Revenue upon the plaintiff of $114,244.40, being 1 per cent tax upon the dividends received by the plaintiff from its subsidiary companies, as before alleged, is unlawful and void, and the collection thereof from the plaintiff was without authority of law, and that there is therefore due from the defendant to the plaintiff the amount thereof, to-wit: $114,244.40, with interest from the date of payment, to-wit: February 17, 1915; for the recovery of which amount the plaintiff brings this, its suit.

REED, SMITH, SHAW & BEAL,
Attorneys for Plaintiff.

14 COMMONWEALTH OF PENNSYLVANIA,
County of Allegheny, ss:

Before me, the undersigned authority, personally appeared G. Webber Barnes, Assistant Treasurer of the Gulf Oil Corporation, who,

being duly sworn, according to law, deposes and says that the averments contained in the foregoing Statement of Claim are true.

[SEAL.] G. WEBBER BARNES.

Sworn to and subscribed before me this 14th day of February, A. D. 1916.

J. H. COWNONER,
Notary Public.

My commission expires January 5, 1919.

EXHIBIT "A."

United States Internal Revenue.

Claim under Series 7, No. 14, for Remission of Taxes Abateable under Section 3220 or Section 3221, R. S., or Section 6, Act of March 1, 1879, as Amended.

STATE OF PENNSYLVANIA,
County of Allegheny, ss:

15 W. J. Guthrie, Secretary of the Gulf Oil Corporation, of the City of Pittsburgh and State and County aforesaid, being duly sworn according to law, deposes and says that Gulf Oil Corporation, a corporation of New Jersey, with offices at Pittsburgh, Pennsylvania, is engaged in the business of holding company; that in the month of December (November list) A. D. 1914, was assessed an internal-revenue tax of $114,034.34 upon its net income for the calendar year 1913, which assessment of the aforesaid tax should, as this deponent verily believes, be abated in part or in whole for the following reasons, viz:

The assessment of $114,034.34 represents a tax of 1 per cent on dividends aggregating $11,424,440.00, less a credit of $210.06 representing an over-assessment on the basis of the return as originally filed by the Corporation. The present claim for abatement, therefore, includes not only the net amount of the assessment, $114,034.34, but the entire amount of the extra assessment amounting to $111,244.40.

The dividends referred to, aggregating $11,424,440.00, were dividends which had been declared and were payable to the Gulf Oil Corporation prior to March 1, 1913, and were paid out of earnings and accrued surplus of subsidiary companies, which had accrued prior to January 1, 1913.

The Gulf Oil Corporation was incorporated February 13, 1907, taking over at that time the stock of the J. M. Guffey Petroleum Company and the Gulf Refining Company, two Texas corporations, incorporated respectively for the purpose of producing and transporting, and refining and marketing petroleum and petroleum

16 products. Subsequently the Gulf Oil Corporation organized two additional subsidiary companies for the purpose of build-

ing and operating pipe lines from its refineries in Texas to the Oklahoma oil fields. These two companies were incorporated as the Gulf Pipe Line Company (of Texas) and the Gulf Pipe Line Company of Oklahoma. The Gulf Oil Corporation also acquired all of the capital stock (except directors' qualifying shares) of the Indiana Oil and Gas Company, a company owning leases and producing oil and gas in the State of Oklahoma. A small merchandising company was also organized at Port Arthur, Texas, known as the Gulf Commissary Company.

From the organization of the Gulf Oil Corporation until December 31, 1912, no dividends were paid by the Gulf Oil Corporation to its stockholders, but the earnings of the subsidiary companies were allowed to accumulate in their respective treasuries.

In January of 1913 the officers of the Gulf Oil Corporation concluded that the accumulated earnings and surplus of the subsidiary companies, not needed for extensions and developments, should be taken over by the Gulf Oil Corporation in the form of dividends, and on February 7, 1913, three of these subsidiary companies namely, the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company (of Texas) and the Gulf Pipe Line Company of Oklahoma, reciting the surplus and accumulated earnings of each of said companies as of December 31, 1912, declared and authorized the payment of dividends to their respective stockholders, as of January 1, 1913. Out of these dividends the Gulf Oil Corporation received the following amounts:

17

From the J. M. Guffey Petroleum Company.....	$3,749,750.00
From the Gulf Pipe Line Company.....	4,724,055.00
From the Gulf Pipe Line Company of Oklahoma..	2,597,660.00
Making	$11,071,465.00

On January 8, 1913, the Indiana Oil and Gas Company, out of its accumulated profit and surplus, declared and authorized the immediate payment of dividends, out of which the Gulf Oil Corporation as a stockholder received $338,000.00; and on February 24, 1913, said Company authorized a dividend, out of which the Gulf Oil Corporation received $10,000.00.

On December 17, 1912, the Gulf Commissary Company, out of the earnings of the company, declared a dividend of 100 per cent, payable out of the net earnings of the company as of December 31, 1912, to stockholders of record as of that date. Of this dividend the Gulf Oil Corporation received $4,975.00.

The dividends above mentioned make up the total amount of $11,412,440.00.

These dividends were forthwith payable, and under the ruling of the Treasury Department, T. D. 2048, were thereupon vested in the stockholder (the Gulf Oil Corporation) on the dates on which said dividends were declared, all of which said dates were prior to March 1, 1913.

It is respectfully contended that such dividends were prop-
18 erly excluded from the original report of the income of the Corporation as filed for the year 1913, and should not now be assessed, for the following reasons:

First. Said dividends were not subject to assessment under Section 38 of the Excise Tax Law of August 5, 1909, for the reason that they consisted of dividends upon stock of other corporations subject to and which had already paid the Excise Tax imposed by said Act.

Second. While it is true that paragraph (T) of the Income Tax Law of October 3, 1913, repeals Sections 1 to 42 of the Act of 1909, and imposes a Special Excise Tax of 1 per cent on the net income of corporations for the months of January and February, 1913, said paragraph provides that the repeal or modification of existing laws embraced in said Act shall not affect any act done or any right accruing or accrued before the said repeal or modification. The right of the Gulf Oil Corporation to receive these dividends in February, 1913, tax free, was a right that had accrued prior to the passage of the Act of 1913, and was not affected by the repeal of the Act of 1909.

Third. These dividends consisted wholly of earnings of subsidiary companies, all the capital stock of which is owned by the Gulf Oil Corporation (except directors' qualifying shares.) The transfer of these earnings to the treasury of the Gulf Oil Corporation by the declaration of dividends in February, 1913, did not in any way change the value of the holdings of the Gulf Oil Corporation; it merely transferred from the treasuries of the subsidiary companies to the treasury of the parent company the accumulated earnings and surplus of previous years; the book value of the stocks owned
19 by the Gulf Oil Corporation being reduced in value the exact amount of the dividends so transferred.

Fourth. The Special Excise Tax for the months of January and February, 1913, provided for in Paragraph (T) of the Income Tax Law of 1913, is not identical and should not be confused with the General Corporation Income Tax provided for in paragraph (G) of said Act. While it is provided that the Special Excise Tax for the two months shall be determined by taking 1-6 of the net income of the corporation for the year, said annual income to be ascertained in accordance with the provisions of sub-section (G) of Section 2 of the Act, this method of ascertaining the amount of the Special Excise Tax can only be used to the extent that the character of the income for the two months is identical with the income for the remaining ten months of the year. In other words, income that was not taxable under either the Act of 1909 or the Special Excise Tax imposed by paragraph (T) of the Act of 1913, can not be made taxable under the general provisions of paragraph (G) of the Act of 1913, by requiring the same to be included in the income report of the company for the entire year and taking 1-6 thereof as the amount of the Special Excise Tax for the two months of January and February.

Fifth. The dividends upon which the present tax is sought to be collected is not income accrued or accruing to the Gulf Oil Corpora-

tion during the calendar year mentioned within the meaning of the Act of Congress.

Sixth. At the date of the approval of said Act, Congress was without power to levy any excise tax upon the Gulf Oil Corporation in respect of income accruing or business done during the months of January and February, 1913; and the Act of 1909 being specifically repealed, there is no authority in law for the making of the present assessment.

Seventh. In any event, no authority exists to impose any other tax during the said months of January and February than that authorized by the said Act of 1909, and this present assessment is entirely without the provisions of the Act.

And this deponent now claims that, for the reasons above stated, it is justly entitled to have $114,034.34 of the aforesaid assessment remitted, and it *now* asks and demands the same.

(Signed) W. J. GUTHRIE,
Secretary Gulf Oil Corporation.

Sworn to and subscribed before me this 5th day of January, A. D. 1915.

(Signed) THOMAS H. BOYD,
Notary Public, Allegheny County, Pa.

My commission expires January 21, 1915.

EXHIBIT "B."

Gulf Oil Corporation.

Pittsburgh, Pa., February 16, 1915.

C. G. Lewellyn, Esq., Collector, Federal Building, Pittsburgh, Penna.

DEAR SIR: The undersigned Corporation pays the Corporation Income Tax assessed against it for the period ending December 31, 1913, amounting to $114,034.34, as per Special Notice of Assessment and Demand dated February 8, 1915, which tax is purported to be levied and assessed in accordance with Section II, Act of Congress of October 3, 1913, and the regulations of the United States Treasury Department issued thereunder, but under protest and reserving to itself all rights to a return, cancellation or modification thereof in the event the said law or said regulations or any part thereof shall be declared to be invalid, void or inoperative, or that any ruling or decision of the Treasury Department affecting said assessment and payment shall be determined to have been incorrect.

GULF OIL CORPORATION,
(Signed) By W. J. GUTHRIE, *Secretary.*

22 EXHIBIT "C."

Claim under Series 7, No. 14, Revised, and Series 7, No. 27, Supplement No. 1, for taxes improperly paid, or refundable under remedial statutes and for amounts paid for stamps used in error or excess.

U. S. Internal Revenue.

STATE OF PENNSYLVANIA,
County of Allegheny, ss:

W. J. Guthrie of the City of Pittsburgh and State and County aforesaid, being duly sworn according to law, deposes and says, that he is Secretary of the Gulf Oil Corporation, a corporation of New Jersey, with offices at Pittsburgh, Pennsylvania, which corporation is engaged in the business of holding company, that upon the 8th day of February, A. D. 1915, the said corporation was assessed an internal-revenue tax of $114,244.40 upon its net income for the calendar year 1913, as per special notice of assessment and demand dated February 8, 1915, and that said corporation afterwards, on the 17th day of February, A. D. 1915, paid under protest to C. G. Lewellyn, Esq., Collector of Internal Revenue for the Twenty-third District of Pennsylvania, the sum of $114,034.34 and was allowed a credit of $210.06 on said assessment, and which amount, as this deponent verily believes, should be refunded for the following reasons, viz:

Because the assessment of said tax against said corporation
23 was illegal and the collection thereof was illegal.

The assessment of $114,034.34 represents a tax of 1 per cent on dividends aggregating $11,424,440.00, less a credit of $210.06 representing an over-assessment on the basis of the return as originally filed by the Corporation. The present claim for the refund, therefore, includes not only the net amount of the assessment, $114,034.34, but the entire amount of the extra assessment amounting to $114,244.40.

The dividends referred to, aggregating $11,424,440.00, were dividends which had been declared and were payable to the Gulf Oil Corporation prior to March 1, 1913, and were paid out of earnings and accrued surplus of subsidiary companies, which had accrued prior to January 1, 1913.

The Gulf Oil Corporation was incorporated February 13, 1907, taking over at that time the stock of the J. M. Guffey Petroleum Company and the Gulf Refining Company, two Texas corporations, incorporated respectively for the purpose of producing and transporting, and refining and marketing petroleum and petroleum products. Subsequently the Gulf Oil Corporation organized two additional subsidiary companies for the purpose of building and operating pipe lines from its refineries in Texas to the Oklahoma oil fields. These two companies were incorporated as the Gulf Pipe Line Company (of Texas) and the Gulf Pipe Line Company of Oklahoma. The

Gulf Oil Corporation also acquired all of the capital stock (except directors' qualifying shares) of the Indiana Oil and Gas Company,
a company owning leases and producing oil and gas in the
24 State of Oklahoma. A small merchandising company was
also organized at Port Arthur, Texas, known as the Gulf Commissary Company.

From the organization of the Gulf Oil Corporation until December 31, 1912, no dividends were paid by the Gulf Oil Corporation to its stockholders, but the earnings of the subsidiary companies were allowed to accumulate in their respective treasuries.

In January of 1913 the officers of the Gulf Oil Corporation concluded that the accumulated earnings and surplus of the subsidiary companies, not needed for extensions and developments, should be taken over by the Gulf Oil Corporation in the form of dividends, and on February 7, 1913, three of these subsidiary companies, namely, the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company (of Texas) and the Gulf Pipe Line Company of Oklahoma, reciting the surplus and accumulated earnings of each of said companies as of December 31, 1912, declared and authorized the payment of dividends to their respective stockholders, as of January 1, 1913. Out of these dividends the Gulf Oil Corporation received the following amounts:

From the J. M. Guffey Petroleum Company.....	$3,749,750.00
From the Gulf Pipe Line Company.....	4,724,055.00
From the Gulf Pipe Line Company of Oklahoma..	2,597,660.00
Making	$11,071,465.00

On January 8, 1913, the Indiana Oil and Gas Company,
25 out of its accumulated profit and surplus, declared and authorized the immediate payment of dividends, out of which the Gulf Oil Corporation as a stockholder received $338,000.00; and on February 24, 1913, said Company authorized a dividend, out of which the Gulf Oil Corporation received $10,000.00.

On December 17, 1912, the Gulf Commissary Company, out of the earnings of the Company, declared a dividend of 100 per cent, payable out of the net earnings of the Company as of December 31, 1912, to stockholders of record as of that date. Of this dividend the Gulf Oil Corporation received $4,975.00.

The dividends above mentioned make up the total amount of $11,442,440.00.

These dividends were forthwith payable, and under the ruling of the Treasury Department, T. D. 2048, were thereupon vested in the stockholder (the Gulf Oil Corporation) on the dates on which said dividends were declared, all of which said dates were prior to March 1, 1913.

It is respectfully contended that the tax assessed should be refunded for the following reasons:

First. Said dividends were not subject to assessment under Section 38 of the Excise Tax Law of August 5, 1909, for the reason that

hey consisted of dividends upon stock of other corporations sub-
ect to and which had already paid the Excise Tax imposed by said
Act.

Second. While it is true that paragraph (S) of the In-
26 come Tax Law of October 3, 1913, repeals Sections 1 to
42 of the act of 1909, and imposes a Special Excise Tax
of 1 per cent on the net income of corporations for the months of
January and February, 1913, said paragraph provides that the repeal
or modification of existing laws embraced in said Act shall not affect
any act done or any right accruing or accrued before the said repeal
or modification. The right of the Gulf Oil Corporation to receive
these dividends in February, 1913, tax free, was a right that had
accrued prior to the passage of the Act of 1913, and was not affected
by the repeal of the Act of 1909.

Third. These dividends consisted wholly of earnings of sub-
sidiary companies, all the capital stock of which is owned by the
Gulf Oil Corporation (except directors' qualifying shares.) The
transfer of these earnings to the treasury of the Gulf Oil Corpora-
tion by the declaration of dividends in February, 1913, did not in
any way change the value of the holdings of the Gulf Oil Corpora-
tion; it merely transferred from the treasuries of the subsidiary
companies to the treasury of the parent company the accumulated
earnings and surplus of previous years; the book value of the stocks
owned by the Gulf Oil Corporation being reduced in value the exact
amount of the dividends so transferred.

Fourth. The Special Excise Tax for the months of January and
February, 1913, provided for in paragraph (S) of the Income Tax
Law of 1913, is not identical and should not be confused with the
General Corporation Income Tax provided for in paragraph (G)
of said Act. While it is provided that the Special Excise Tax for
the two months shall be determined by taking 1/6 of the net in-
come of the corporation for the year, said annual income to
27 be ascertained in accordance with the provisions of sub-section
(G) of Section 2 of the Act, this method of ascertaining the
amount of the Special Excise Tax can only be used to the extent
that the character of the income for the two months is identical
with the income for the remaining ten months of the year. In
other words, income that was not taxable under either the Act of
1909 or the Special Excise Tax imposed by paragraph (T) of the
Act of 1913, can not be made taxable under the general provisions
of paragraph (G) of the Act of 1913 by requiring the same to be
included in the income report of the company for the entire year
and taking 1/6 thereof as the amount of the Special Excise Tax
for the two months of January and February.

Fifth. The dividends upon which the present tax is sought to be
collected is not income accrued or accruing to the Gulf Oil Corpora-
tion during the calendar year mentioned, within the meaning of the
Act of Congress.

Sixth. At the date of the approval of said Act, Congress was
without power to levy any excise tax upon the Gulf Oil Corporation
in respect of income accruing or business done during the months

of January and February, 1913; and the Act of 1909 being specifically repealed, there is no authority in law for the making of the present assessment.

Seventh. In any event, no authority exists to impose any other tax during the said months of January and February than that authorized by the said Act of 1909, and this present assessment is entirely without provisions of the Act.

28 And this deponent now claims that, by reason of the payment of the said sum of $114,034.34 and the allowance of a credit of $210.06, the said corporation is justly entitled to have the sum of $114,034.34 and $210.06 refunded, and it now asks and demands the same.

And this deponent further makes oath that the said claimant is not indebted to the United States in any amount whatever, and that no claim has heretofore been presented for the refunding of the above amount, or any part thereof.

(Signed) W. J. GUTHRIE.

Sworn to and subscribed before me this 27th day of February, A. D. 1915.

[N. P. Seal.]

(Signed) J. K. CROWNOVER,
Notary Public.

My commission expires January 5, 1919.

29 EXHIBIT "D."

Treasury Department,

Internal Revenue Service.

Pittsburgh, Pa., April 13th, 1915.

Income Tax.

Gulf Oil Corporation, Pittsburgh, Pa.

SIRS: This office is in receipt of Department letter dated April 9th, 1915, which reads as follows:

"The claim of the Gulf Oil Corporation of Pittsburgh, Pa., for the refunding of $114,244.40, claimed to have been paid in error as corporation income taxes on account of the year 1913, has been examined.

Claims for the abatement of these taxes were rejected in this office on October 29th, 1914, and February 4th, 1915, for the reason that the amounts involved represented 1 per cent of the amounts received by claimant during 1913 as dividends from other corporations.

30 Claimant contends that as the dividends in question were received prior to March 1, 1913, the corporation should receive the same tax free. As you were advised in office letter

of February 4, 1915, the Act of October 3, 1913, provides that the tax for January and February, 1913, shall be computed and the net income ascertained in accordance with the provisions of sub-section G of section 2, which section does not provide for the deduction from gross income of dividends received from other corporations paying a like tax. On February 3, 1915, this case was heard before the Solicitor of Internal Revenue, who concurred, after a full hearing and consideration of all the facts, in the opinion that the tax was legally assessed. There has been no new material evidence presented with the refunding claim, and as the evidence on file establishes the company's liability to this tax, the claim is hereby rejected.

You will please notify claimant of this action, returning the receipts on Form 1, which are herewith enclosed."

Receipts on Form 1 are herewith enclosed.

Yours very truly,

C. G. LEWELLYN, *Collector.*

31 *Affidavit of Defense.*

Filed March 15, 1916.

UNITED STATES OF AMERICA,
Western District of Pennsylvania, ss:

C. G. Lewellyn, Collector, and Defendant above named, being duly sworn according to law, deposes and says that he has a just, full and complete defense to the whole of Plaintiff's claim embodied in the statement filed in this case, the nature and character of which is as follows:

First to Ninth. Defendant admits the averments of fact contained in paragraphs number first to ninth, inclusive, in the statement of claim, except that there is an error in figures in the second paragraph thereof, the correct amount of dividends received by Plaintiff being $11,424,440.00 instead of $11,424,000.00.

Tenth. Defendant admits that Plaintiff is a holding company as alleged in the tenth paragraph of Plaintiff's statement. Defendant denies, however, that no dividends were paid by any of the subsidiary companies (with the exception of the Indiana Oil and Gas Company and the Gulf Commissary Company) prior to December 31, 1912, but on the contrary avers that in the year 1912, a dividend amounting to $2,024,865.00 was paid by the J. M. Guffey Petroleum Company to the Plaintiff.

32 Eleventh. Defendant admits the averments contained in the eleventh paragraph of Plaintiff's statement of claim, but avers that Plaintiff did not receive payment of the dividend in question until April 11, 1913.

Twelfth. Defendant admits the averments in the twelfth paragraph of Plaintiff's statement of claim, but avers that Plaintiff did not receive payment of the dividend in question until April 11, 1913.

Thirteenth. Defendant admits the averments contained in the thirteenth paragraph of Plaintiff's statement of claim, but avers that Plaintiff did not receive payment of the dividend in question until April 11, 1913.

Fourteenth. Defendant admits the averments contained in the fourteenth paragraph of Plaintiff's statement of claim. Defendant avers that Plaintiff received payment of the dividend declared on January 8, 1913, on the same day, and that the Plaintiff received payment of the dividend declared on February 24, 1913, on the 25th day of February, 1913.

Fifteenth. Defendant admits the averments contained in the fifteenth paragraph of Plaintiff's statement of claim but avers that Plaintiff did not receive payment of the dividend in question until January 4, 1913.

Sixteenth. Defendant is without knowledge as to whether the said five corporations had paid all of the taxes imposed upon them under the provisions of the Act of Congress of August 5,
33 1909, and as to whether the earnings from which said dividends were declared had been taxed under the provisions of said Act of Congress. If these allegations of the statement of claim are material to the issue, Defendant demands proof thereof at the trial of this case. Defendant is advised however, and therefore avers that the said allegations are wholly immaterial to any issue involved in this case.

Seventeenth. Defendant denies all the allegations contained in the seventeenth paragraph of the Plaintiff's statement of claim.

Eighteenth. Defendant denies all the allegations contained in the eighteenth paragraph of the Plaintiff's statement of claim.

For further answer to Plaintiff's statement of claim, Defendant avers that the taxes, for recovery of which Plaintiff brought this suit, were legally assessed against and collected from the Plaintiff under authority of the laws of the United States, particularly the Act of Congress approved October 3, 1913, 38 Stat. 166, and therefore the Defendant is not indebted to the Plaintiff in the sum of $114,244.40, or any other sum.

Defendant avers that Plaintiff's statement of claim does not set forth a cause of action and should therefore be dismissed at Plaintiff's cost.

Deponent avers that all the facts herein set forth are true.

C. G. LEWELLYN.

Sworn to and subscribed before me this 15th day of March, A. D., 1916.

[SEAL.]

G. L. BERGER,
Deputy Clerk United States
District Court, Pittsburgh, Pa.

34 *Præcipe for Trial List.*

Filed August 22, 1916.

To J. Wood Clark, Esq., Clerk.

SIR: Place the above entitled case on the next trial list.

REED, SMITH, SHAW & BEAL,
Attorneys for Plaintiff.

August 21, 1916.

Stipulation Waiving a Jury Trial.

January 16, 1917.

And now, to wit, January 16th, 1917, we, the parties to the above entitled cause, by our attorneys, hereby waive the trial to the jury of this cause and agree that the issues involved in said cause be tried and determined by the Court without the intervention of a jury; however reserving to us and each of us the right to procure a review by an appeal or writ of error.

35 REED, SMITH, SHAW & BEAL,
Attorneys for Plaintiff.

B. B. McGINNIS,
Attorney for Defendant.

Trial Memorandum.

Filed January 30, 1917.

No. 1592, May Term, 1916.

GULF OIL CORPORATION

vs.

C. G. LEWELLYN, Collector.

Trial without jury.
Witnesses: Walter J. Guthrie, for Plaintiff.

36 *Testimony.*

Heard before Honorable Charles P. Orr, on Tuesday, January 30th, 1917, at Pittsburgh, Pennsylvania.

Appearances:

Messrs. Reed, Smith, Shaw & Beal, for Plaintiff.
B. McGinnis, Esq., Special Assistant United States Attorney; B. M. Price, Esq., Assistant United States Attorney for Defendant.

For the purpose of this case, the following facts are admitted by the counsel for the respective parties, viz:

"First. The Gulf Oil Corporation is a corporation duly organized under the laws of the State of New Jersey. C. G. Lewellyn is the Collector of Internal Revenue for the Twenty-third District of Pennsylvania, being duly commissioned as such pursuant to the laws of the United States of America.

Second. The Gulf Oil Corporation, on the 14th day of February, 1914, in compliance with the provisions of the Act of Con-
37 gress of October 3, 1913, made a return of its annual net income for the twelve months ending December 31, 1913, as required by said Act. In making said return the Gulf Oil Corporation certified that it had not included in the statement of gross income for the year 1913 certain dividends amounting to $11,424,440.00 received by it from subsidiary companies out of earnings and surplus of said subsidiary companies accrued prior to January 1, 1913.

Third. In said return the Gulf Oil Corporation showed net income for the twelve months ending December 31, 1913, of $886,250.44, but under date of May 1, 1914 the said C. G. Lewellyn, Collector, mailed to said corporation notice of an assessment of tax thereon amounting to $9,072.56. A claim for abatement of his overcharge, amounting to $210.06, was filed with the Collector June 9, 1914, and on June 30, 1914, the Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, the sum of $8,862.50, being the amount of said assessment, less the $210.06 for which abatement was claimed. Said claim for abatement having been disallowed, said Gulf Oil Corporation, on the 5th day of November, 1914, paid the said Collector the additional sum of $210.06, with interest amount to $6.30, making a total payment of $216.36.

Fourth. On the 30th day of December, 1914, the said C. G. Lewellyn, Collector, acting under instructions from the Commissioner of Internal Revenue at Washington, D. C., mailed notice and demand for tax assessment against the Gulf Oil Corporation for the year ending December 31, 1913, amounting to $114,034.34.
38 In fact, this additional assessment amounted to $114,244.40, being the 1 per cent upon the entire amount of the dividends received by the Gulf Oil Corporation from subsidiary companies out of surplus accrued to such subsidiaries prior to January 1, 1913, and payable to the Gulf Oil Corporation prior to March 1, 1913, and said additional assessment was based solely on said dividends. In making the assessment, however, the Commissioner of Internal Revenue reconsidered and allowed the previous claim for abatement of $210.06, erroneously assessed against the corporation in the original assessment, and credited the same as having been paid upon the assessment of December 30, 1914, leaving the net balance of such assessment $114,034.34 as stated.

Fifth. The notice and demand of the said C. G. Lewellyn, Collector, for the payment of this additional tax recites that if the tax is not paid on or before January 8, 1915, it would be the duty of the

Collector to collect said tax, together with 5 per cent additional and interest at the rate of 1 per cent per month until paid.

Sixth. That subsequently the plaintiff filed with the defendant for presentation to the Commissioner of Internal Revenue a claim for the abatement of said income tax amounting to $114,034.34, a copy of which claim is attached to and made a part of plaintiff's statement as Exhibit A. That after an examination of said claim for abatement the Commissioner of Internal Revenue rejected the same.

39 Seventh. On February 17, 1915, the said Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, said additional income taxes assessed for the period ending December 31, 1913, in the sum of $114,034.34, and at the same time filed with said C. G. Lewellyn a written protest, a copy of which protest is attached to and made a part of plaintiff's Statement as Exhibit B.

Eighth. That subsequently the plaintiff filed with the said C. G. Lewellyn, for presentation to the Commissioner of Internal Revenue a claim for the refund of the net amount of the assessment of said income tax, to wit: $114,034.34, and also the amount of the credit allowed thereon of $210.06, representing an over assessment against the corporation on the basis of its return as originally filed, the two amounts constituting the entire amount of the additional assessment in the sum of $114,244.40. A copy of the said claim for refund is attached to and a part of plaintiff's Statement as Exhibit C.

Ninth. That after consideration of said claim for refund, the Commissioner of Internal Revenue rejected the same, and the said C. G. Lewellyn was instructed to notify the Gulf Oil Corporation, and on or about April 13, 1915, did so notify said corporation, that said claim was rejected, a copy of which notice is attached to and made a part of plaintiff's Statement as Exhibit D.

Tenth. The plaintiff is a holding company, and continuously since its organization in February, 1907, it has been the owner of all of the capital stock of the J. M. Guffey Petroleum Com-

40 pany, the Gulf Pipe Line Company, the Gulf Pipe Line Company of Oklahoma, and for many years has been the owner of all of the capital stock of the Indiana Oil and Gas Company and the Gulf Commissary Company, except in the case of each company of directors' qualifying shares, and was the owner of said shares during all the period in which the earnings have accumulated out of which the dividends in question in this case were declared and paid.

That with the exception of the Indiana Oil & Gas Company and the Gulf Commissary Company and a dividend of the J. M. Guffey Petroleum Company hereafter referred to, no dividends were paid by any of the above-named subsidiary companies prior to December 31, 1912. All of the earnings of said companies prior to said date were either invested as earned in the extension and development of the properties and business of the companies mentioned or allowed to accumulate in the treasuries of such companies respectively, and all of the said earnings were actually used and required in carrying on the business of the subsidiary companies.

In January of 1913 the officers of the Gulf Oil Corporation, plaintiff, decided that the accumulated earnings and surpluses of these subsidiary companies should be taken over by the plaintiff company in the form of dividends and accordingly:

Eleventh. On February 7, 1913, the J. M. Guffey Petroleum Company declared and authorized out of its accumulated
41 surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $3,749,750.00. Payment of said dividend was made April 11, 1913.

Twelfth. On February 7, 1913, the Gulf Pipe Line Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $4,724,055.00. Payment of said dividend was made April 11, 1913.

Thirteenth. On February 7, 1913, the Gulf Pipe Line Company of Oklahoma declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $2,597,660.00. Payment of said dividend was made April 11, 1913.

Fourteenth. On January 8, 191 , the Indiana Oil and Gas Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Company received $338,000.00; and on February 24, 1913, declared and authorized the immediate payment of a dividend, of which the Gulf Oil Corporation received $10,000.00. Payment of the dividend declared January 8, 1913, was made on that day and payment of the dividend declared February 24, 1913, was made on February 25, 1913.

Fifteenth. On December 17, 1912, the Gulf Commissary Company declared and authorized out of its accumulated surplus
42 earned prior to December 17, 1912, the payment of a dividend, of which the Gulf Oil Corporation received $4,975.00. Payment of said dividend was not made until January 4, 1913."

Recess.

Afternoon Session.

WALTER J. GUTHRIE, a witness called on behalf of plaintiff, having been duly sworn, testified as follows:

Direct examination.

Mr. Beal:

Q. By profession you are an attorney?

A. An attorney-at-law, yes, sir.

Q. You are secretary of the Gulf Oil Corporation, the plaintiff in this case?

A. Yes, sir.

Q. How long have you been secretary of that company?
A. Since 1907.
Q Substantially since the organization of that corporation?
A. Yes, sir.
Q. Are you also secretary of the various subsidiary companies of that corporation?
A. All that contributed to this dividend, except the Indiana Oil and Gas Company.
43 Q. Then, with the exception of the Indiana Oil and Gas Company, you are secretary of the other companies that have been mentioned here?
A. Yes, sir.
Q. Do you have possession of the minute books of such of the companies as existed anterior to the time when you became secretary of the Gulf Oil Corporation?
A. I have.
Q. You are familiar, are you, with the affairs of the companies then from their inception, in a general way?
A. Yes, sir.
Q. The Gulf Oil Corporation itself, I believe, is a holding company?
A. Yes, sir.
Q. It owns the shares of stock of the various subsidiary companies?
A. Yes, sir.
Q. It does no business itself excepting the management of its interests as stockholder in these various companies?
A. That is all.
Q. Without giving us the names and details, the Gulf Oil Corporation is engaged in an oil enterprise?
A. Yes, sir.
Q. And that extends, does it, from the production of oil, its transportation by pipe lines, the refining of the oil and the marketing of the refined oil and its products?
A. Yes, sir.
Q. Then, as to these subsidiary companies, do you have separate subsidiaries for the carrying on of the producing portion of
44 the enterprise?
A. We do.
Q. And those producing companies do they also purchase?
A. They do not purchase now.
Q. Then the Pipe Line Companies receive it from the producing companies?
A. Yes.
Q. And transport it to the refinery and on to the point of sale?
A. Yes, sir.
Q. And they conduct the gathering of the oil in the various fields, I take it?
A. Yes, sir.
Q. Then do they also purchase oil?
A. They do.

Q. The refineries of the enterprise are located where?
A. Port Arthur and Fort Worth, Texas.
Q. Where are the producing fields and the fields in which the company buys oil?
A. Principally the coastal fields of Texas.

Mr. McGinnis: We would like counsel to be a little more specific.
Mr. Beal: I am referring now, of course, when I speak of the producing companies, to the subsidiary companies.

45 Mr. Beal:

Q. What about the Oklahoma field?
A. That was only part of the answer. The coastal fields of Texas, the fields of Louisiana and the oil fields of Oklahoma.

Mr. McGinnis: What company are you now referring to?

Mr. Beal:

Q. What companies perform that part of the enterprise?
A. The Gulf Refining Company of Louisiana in Louisiana, the Gulf Production Company, formerly the J. M. Guffey Petroleum Company, of Texas, and the Gypsy Oil Company of Oklahoma.
Q. The Gypsy Company and the Gulf Refining Company of Louisiana are not particularly a question in this case?
A. No, sir.
Q. The Gulf Refining Company then gets the oil at the refineries and carries on the manufacturing processes?
A. Yes, sir.
Q. And how about the marketing; does it also carry on the marketing?
A. The Gulf Refining Company carries on the marketing in all States except a few Southern States that are covered by the Gulf Refining Company of Louisiana, which is also a subsidiary.
Q. Are all of these companies that you have mentioned, subsidiary companies carrying on the enterprise of the Gulf Oil Corpo-
46 ration?
A. They are.
Q. And the Gulf Oil Corporation owns, does it, all the shares of stock of those companies except the necessary qualifying shares for directors?
A. It does. I might also state that the Indiana Oil and Gas Company is a subsidiary company in Oklahoma.
Q. Prior to the payment of the dividends in question here, which were declared in January and February, 1913, had any of these companies which make up this enterprise, paid any dividends to their stockholders?
A. None, with the exception of the J. M. Guffey Petroleum Company.
Q. When was that dividend declared?
A. On December 22, 1911.
Q. Will you tell us the circumstances under which that dividend

was declared, or, let me put it this way: Prior to the declaration of that dividend the J. M. Guffey Petroleum Company owned a fleet of steamships?

A. Yes, sir.

Q. Which were used in the transportation of oil from the refinery to the market?

A. Yes, sir.

Q. Was that fleet sold?

A. It was.

Q. At what time?

A. The transfer of the fleet was ratified at this meeting of December 22nd, 1911.

Q. Sold to the Gulf Refining Company?

A. Yes, sir.

Q. And continued to be used in the same business as used
47 before?

A. Exactly. The ownership was simply transferred from one subsidiary company to the other.

Q. The interest of the Gulf Oil Corporation in these two companies being the same?

A. Exactly the same.

Q. Now, then, as to this dividend, will you tell us the amount of the dividend and its purpose?

A. At that meeting, after the transfer of the fleet the Guffey Petroleum Company to the Gulf Refining Company was ratified and approved, the Corporation, that is, the J. M. Guffey Petroleum Company, declared a dividend of $13.50 per share, which practically represented the purchase price of the fleet.

Q. Then what was done with——

A. That dividend, of course, came into the treasury of the Gulf Oil Corporation as a dividend from its subsidiary, the J. M. Guffey Petroleum Company, and the Gulf Oil Corporation then furnished to the Gulf Refining Company the money with which to pay the J. M. Guffey Petroleum Company for the ships.

Q. The amount being identical?

A. It may not be the exact amount in dollars, but substantially identical.

Q. Was it intended to be a distribution of the proceeds of the sale of the ships?

A. Yes, sir.

Q. And following that when the company was able to do so, was the capital stock of the company reduced?

A. Yes, sir.

Q. And following that when the company was able to do so, was the capital stock of the company reduced?

48 *A. Yes, sir.*

Q. That is, the capital stock of the J. M. Guffey Petroleum Company?

A. Yes, sir.

Q. From the time at which a tax was assessed by the United States upon the earnings of corporations, by the Act of 1909, down to and

including all of the earnings that accrued prior to January 1st, 1913, did these subsidiary companies which declared the dividends that are in question here, pay a tax upon those earnings?

A. They did. It was an excise tax.

Q. Without going into details, you had charge of the matter of the returns, had you?

A. Yes, sir.

Q. And seeing that the taxes were paid?

A. Yes, sir.

Q. They made their reports as provided by law?

A. They did.

Q. Did the officers of the Government examine the books and verify the correctness of them?

A. They did.

Q. And the entire amount was paid?

A. It was.

Q. And has there ever been any question raised by the Government about their having paid taxes on all earnings that were subject to taxation?

A. It never has.

Q. No dividends being declared by these various subsidiary companies as you have mentioned, I wish you would state whether the company did make large earnings in its properties prior to January 1st, 1913?

A. It did.

49 Q. Coming now to the 31st of December, 1912, and the accumulated surpluses that were dealt with by the defendant's declarations in question, were those earnings or surpluses in the subsidiary companies in the shape of cash, or were they in use in the business of the companies and represented by properties of various kinds?

A. They had been reinvested continuously as earned in property and extensions of the various companies.

Q. As I understand, the earnings were not necessarily reinvested in the business of the particular subsidiary that may have made the earnings, but may have been invested in the properties and business of some other of the subsidiaries, there existing a debtor and creditor account as between the two subsidiaries. Would that be correct?

A. That is substantially correct, yes.

Q. For purposes of illustration to avoid going into details, the accounting of these companies was carried on as though they represented entirely distinct and different ownerships?

A. Yes, sir.

Q. Take the case of the Gulf Refining Company and the Gulf Pipe Line Company, the Pipe Line Company, I take it from your description, supplied oil to the Refining Company?

A. Yes, sir.

Q. In that way the Refining Company in the refining and marketing of oil, had a very large investment, I take it, in plants and properties wherever you marketed the oil?

A. Yes, sir.

Q. By the way, where did the company market its oil? Was it local or extensive?

50 A. It was all over the eastern part of the United States and in foreign countries.

Mr. McGinnis: What company?

A. The Gulf Refining Company. The Gulf Refining Company of Louisiana marketed only in three or four of the Southern States.

Mr. Beal:

Q. And in the marketing of the oil is or is not the company involved in a large investment for that purpose in taxes, stations, delivery conveyances, and various kinds?

A. Yes, sir, very largely.

Q. When these dividends were declared, I wish you would tell me how the transaction was handled, as to whether they were paid in money and received as such by the Gulf Oil Corporation.

A. The dividends were paid by checks, in order to make book entries to correspond with the declaration of the dividends, and the corresponding entries were made on the books of the subsidiary companies, showing the payment of these dividends, and entries were made on the Gulf Oil Corporation records showing the receipt of these dividends. Of course, corresponding items of indebtedness appear upon the books of the subsidiary companies to represent the amount of the dividends. It was a book-keeping transaction.

Q. Take as an illustration, the case of the one I referred to, the Gulf Refining Company and the Gulf Pipe Line Company. The Gulf Refining Company owed the Gulf Pipe Line Company at that time a large amount of money—do you recall the amount?

A. I can't give you the amount, no sir.

51 Q. The Gulf Pipe Line Company was one of the companies declaring the dividends?

A. Yes, sir.

Q. That dividend amounted to forty-seven hundred and odd thousand dollars. Now what I want to get at is, where did the Gulf Pipe Line Company get the money to pay that dividend?

The Court: Has not the witness stated these dividends were not paid in money?

The Court:

Q. As I understand it, this was a bookkeeping arrangement purely?

A. Exactly.

Q. The dividend was declared and effected a distribution of assets?

A. Yes, sir.

Q. Was that a distribution of accumulated assets which were profits in operation?

A. Yes, sir.

Q. You didn't have the money with which to pay the dividends; is that right?

A. Yes, sir.

Q. And among the assets which went to make the accumulated profits, were the accounts receivable and bills receivable of the other companies?

A. That is true, yes sir.

Q. And in the declaration of the dividend there was a check passed and followed by the cancellation or payment of some of the accounts receivable or bills receivable, or whatever it was, held by the company that declared the dividend—the bills payable?

52 A. The bills payable and receivable were rearranged among the subsidiary companies, and it was a bookkeeping transaction.

Mr. Beal:

Q. And with this change, when the transaction was concluded, the subsidiary companies treated them all collectively, owed all book accounts to the Gulf Oil Corporation in about the same amount that had theretofore been owing as between the subsidiaries themselves?

A. I couldn't answer that question.

Q. Approximately that?

A. Approximately they owed to the Gulf Oil Corporation the exact amount of this dividend.

Cross-examination.

Mr. McGinnis:

Q. You say you are secretary of all of these companies involved in this suit except the Indiana Oil and Gas Company?

A. Yes, sir.

Q. Do they have regular meetings of their boards of directors?

A. Not in the sense of having monthly meetings. Their meetings are irregular, but they have frequent meetings.

Q. Do you act as secretary at all of these meetings?

A. I do.

Q. You stated that the Gulf Oil Corporation does not do any business except look after its stock interests?

A. That is all.

53 Q. Has the Gulf Oil Corporation any other stock besides those that are involved in this suit?

A. Yes, sir.

Q. Has it any other interests?

A. Well, I will have to understand exactly your question. There are a number of subsidiary companies that I have already mentioned, that are not involved in this suit, but they are part of this one single enterprise of this oil business. It owns no stocks outside of this particular enterprise.

Q. You spoke of the Gulf Oil Company of Louisiana, which is not involved in this suit. Did you receive any dividends from that corporation in the year 1913?

A. No, sir.
Q. Did you receive any other dividends besides those in question, in the year 1913—that is, the Gulf Oil Corporation?
A. Subsequent to this, yes.

Mr. Beal: Their report shows that they did.

(Question read.)
A. I might modify that. I can't remember whether we received any in 1913 or not, until I look at one of the reports.

Mr. McGinnis:

Q. I don't care anything about the amount.
A. We probably did, yes. There were dividends declared subsequent to the income tax law and subsequent to March 1st, so they are not involved in this question. They were reported in the
54 report for 1913.
Q. Did the Gulf Oil Corporation own any property besides stock?
A. I believe nothing except some office furniture in the Pittsburgh office.
Q. I understand you to say the Gulf Oil Corporation did refining?
A. No, sir. The Gulf Refining Company.
Q. You stated that in 1911 the J. M. Guffey Petroleum Company declared a dividend?
A. Yes, sir.
Q. Who received that dividend?
A. The Gulf Oil Corporation received all of it except the small amount payable to the directors on their qualifying shares.
Q. You also stated the capital stock of the Guffey Petroleum Company was reduced at the time they sold their ships——
A. Not until some time after. The proposed reduction was in contemplation at that time, but was not effected until the last of its bonds were paid off a year or so later; then it was reduced.
Q. That was an entirely separate transaction, the reduction in stock, and separate from the amount that was paid for the ships?
A. I don't understand your question.
Q. I understand you bought the ships, the Gulf Oil Corporation bought the ships from the J. M. Guffey Petroleum Company.
A. Yes.
Q. How did they pay for them?
A. They borrowed the money from the Gulf Oil Corporation.
Q. How did they pay for them?
55 A. They paid for them by voucher, and then they declared the proceeds of that out in this dividend of 1911 that I have testified to. So that the proceeds came back into the treasury of the Gulf Oil Corporation.
Q. You stated that the subsidiary companies here involved paid taxes on their earnings, under the Act of 1909, up to the year 1913?
A. Yes, sir.
Q. Did the Gulf Oil Corporation pay any tax under the Act of 1909 on its earnings?

A. It did.

Q. What amount?

A. On 1913?

Q. No, up to that, previous to the year 1913.

A. It paid—the only year it showed any earnings subject to tax was 1913; it paid on $886,250.44.

Q. That isn't what I asked you. I asked you if previous to the year 1913 the Gulf Oil Corporation ever paid any tax?

A. There were no earnings upon which to pay taxes. Its reports for 1909, 1910, 1911 and 1912 show no taxes due.

Q. You stated that the dividends were paid by checks in these subsidiary corporations?

A. Yes, sir.

Q. What did you do with those checks?

A. They were passed through the bank by the Gulf Oil Corporation.

Q. And cashed?

A. Yes, they were cashed by the bank, by offsetting accounts.

Q. But the checks were paid in the usual manner, cashed,
56 and you got a credit for that amount?

A. I believe they were.

Q. How did you arrange the bills receivable of these subsidiary corporations, and then for these subsidiary corporations declare a dividend, and at the same time have the subsidiary corporations owe the same amounts to the Gulf Oil Corporation?

A. They didn't owe the same amount to the Gulf Oil Corporation. The Gulf Oil Corporation practically advanced to the subsidiary companies the money necessary. The subsidiary companies paid a dividend, the money was received by the Gulf Oil Corporation, and the net result was that the bills receivable of the Gulf Oil Corporation were increased the amount of the dividend, and the bills payable of the subsidiary companies were increased the exact same amount.

Q. But the subsidiary companies were allowed to retain their earnings that they had placed in equipment or what not—they were allowed to retain that property, and had paid besides that eleven million dollars of dividends to the Gulf Oil Corporation?

A. The property of the subsidiary companies was not at all disturbed, and neither was the value of the assets of the Gulf Oil Corporation changed, because what had previously been represented in the value of the stock of the subsidiaries was now that much less in value of stock, but that much more in receivables of the subsidiaries.

Q. That happens in every transaction, in every dividend, does it not?

A. No. In the ordinary dividend the value of the stock is decreased and the money is dissipated to the various stockholders. Where it goes into the treasury of a holding company, it is a different proposition; it still remains in the enterprise.

57 Q. You owed the Gulf Oil Corporation eleven million dollars more than you ever did before?

A. The subsidiary companies did, but they owed it to themselves in the sense that the Gulf Oil Corporation*ed* owned them.

Q. You might regard it as such, but we want to get at how they handle their business. So that you owed the Gulf Oil Corporation eleven million dollars more than you ever did, the subsidiary corporations?

A. That is true. The subsidiary companies had increased their debt the amount of this dividend.

Q. There must have been eleven million dollars of assets wiped out some place?

A. No. The debt of the subsidiary companies was increased, but that increased indebtedness was owed to the Gulf Oil Corporation, which owned the subsidiary.

Q. So in effect, here is what happened: you paid a dividend of eleven million dollars from the subsidiary companies; the value of the stock didn't vary one iota?

A. Yes, the value of the stock was reduced; the book value of the stock wasn't, but what had previously been considered as capital stock value had now become a bills payable. The value of the stock in the Gulf Oil Corporation remained the same.

Q. Did you reduce the capital stock of the subsidiary companies any?

A. No, sir.

Q. They remained the same?

A. There was no reduction made on account of this dividend. The stock of the J. M. Guffey Petroleum Company was reduced, but for another reason altogether and had nothing to do with this.

58 Q. Did this transaction, the declaring of a dividend by the subsidiary companies, reduce the value of the stock of the subsidiary company which was so reduced, more than what the stock originally cost?

Mr. Beal: Objected to as irrelevant.

The Court: How is that material and relevant?

Mr. McGinnis: We want to find out how much the stock was reduced and whether it took any of their invested capital.

The Court: He doesn't contend that there was a depletion of capital in any case, except in the case of the J. M. Guffey Company.

Mr. McGinnis:

Q. You stated that the subsidiary companies were, of course, involved in business transactions between each other and paid money to each other, borrowed money of each other and paid it back, etc.?

A. Yes, sir.

Q. Were the directors of all these subsidiary corporations and the Gulf Oil Corporation identical?

A. Not identical, no. The stockholdings were as I have stated. The Gulf Oil Corporation owned all the stock of these subsidiaries involved in this transaction, with the exception of one share each to the qualifying directors.

59 Q. Each subsidiary corporation and the Gulf Oil Corporation as well, had a set of directors of its own and they were not identical?

A. They were not entirely identical. They were made up of the same group, but they were not the same in each case. That is correct.

Q. Are you sure about the Gulf Oil Corporation owning all these shares of stock except the qualifying shares, of the Indiana Oil and Gas Company?

A. Yes, sir.

Q. The moneys that you spoke of as being invested by the subsidiary corporations and loaned to one another, etc., was the money so invested by these subsidiary corporations in the line of their endeavor or business, or was it the money invested indiscriminately in whatever the collective corporation wanted? In other words, if the Pipe Line Company wanted to buy pipe would they buy their own pipe?

A. Yes.

Q. If they didn't have the money, they might borrow it from some other corporation?

A. Yes.

Q. And if another corporation wanted to invest in drilling equipment, they would invest their own money in the drilling equipment?

A. Yes, sir.

Plaintiff rests.

Testimony closed.

60 Mr. McGinnis: We have nothing to offer.

Testimony closed.

Certificate.

I hereby certify that the foregoing is a true transcript of all the evidence taken in the case of Gulf Oil Corporation vs. C. G. Lewellyn, Collector of Internal Revenue, at November 1592 *May* Term, 1916.

L. D. IAMS,
Official Reporter,
By M. GANGWISCH.

Pittsburgh, Pa., April 30, 1917.

Certificate.

I, Charles P. Orr, Judge of the District Court of the United States for the Western District of Pennsylvania, certify that the foregoing is a correct transcript of all the evidence taken in the case of Gulf Oil Corporation vs. C. G. Lewellyn, Collector of Internal Revenue, at No. 1592 November Term, 1916.

CHARLES P. ORR,
Trial Judge.

Pittsburgh, Pa., April 30, 1917.

61 *Request for Findings of Fact and Conclusion of Law.*

Filed January 30, 1917.

Plaintiff's counsel respectfully request the Court to make the following findings of fact:

First. The Gulf Oil Corporation is a corporation duly organized under the laws of the State of New Jersey. C. G. Lewellyn is the Collector of Internal Revenue for the Twenty-third District of Pennsylvania, being duly commissioned as such pursuant to the laws of the United States of America.

Second. The Gulf Oil Corporation, on the 14th day of February, 1914, in compliance with the provisions of the Act of Congress of October 3, 1913, made a return of its annual net income for the twelve months ending December 31, 1913, as required by said Act. In making said return the Gulf Oil Corporation certified that it had not included in the statement of gross income for the year 1913 certain dividends amounting to $11,424,440.00 received by it from subsidiary companies out of earnings and surplus of said subsidiary companies accrued prior to January 1, 1913.

Third. In said return the Gulf Oil Corporation showed net income for the twelve months ending December 31, 1913, of $886,250.44, but under date of May 1, 1914, the said C. G. Lewellyn, Collector, mailed to said corporation notice of an assessment of tax thereon amounting to $9,072.56. A claim for abatement of this overcharge, amounting to $210.06, was filed with the collector June 9,

62 1914, and on June 30, 1914, the Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, the sum of $8,862.50, being the amount of said assessment, less the $210.06 for which abatement was claimed. Said claim for abatement having been disallowed, said Gulf Oil Corporation, on the 5th day of November, 1914, paid the said Collector the additional sum of $210.06, with interest amounting to $6.30, making a total payment of $216.36.

Fourth. On the 30th day of December, 1914, the said C. G. Lewellyn, Collector, acting under instructions from the Commissioner of Internal Revenue at Washington, D. C., mailed notice and demand for tax assessment against the Gulf Oil Corporation for the year ending December 31, 1913, amounting to $114,034.34. In fact, this additional assessment amounted to $114,244.40, being the 1 per cent upon the entire amount of the dividends received by the Gulf Oil Corporation from subsidiary companies out of surplus accrued to such subsidiaries prior to January 1, 1913, and payable to the Gulf Oil Corporation prior to March 1, 1913, and said additional assessment was based solely on said dividends. In making the assessment, however, the Commissioner of Internal Revenue reconsidered and allowed the previous claim for abatement of $210.06, erroneously assessed against the corporation in the original assessment, and credited the same as having been paid upon the assessment of December 30, 1914, leaving the net balance of such assessment $114,034.34 as stated.

Fifth. The notice and demand of the said C. G. Lewellyn, Collector, for the payment of this additional tax recites that if the tax is not paid on or before January 8, 1915, it would be the duty
63 of the Collector to collect said tax, together with 5 per cent additional and interest at the rate of 1 per cent per month until paid.

Sixth. That subsequently the plaintiff filed with the defendant for presentation to the Commissioner of Internal Revenue a claim for the abatement of said income tax amounting to $114,034.34, a copy of which claim is attached to and made a part of plaintiff's Statement as Exhibit A. That after an examination of said claim for abatement the Commissioner of Internal Revenue rejected the same.

Seventh. On February 17, 1915, the said Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, said additional income taxes assessed for the period ending December 31, 1913, in the sum of $114,034.34, and at the same time filed with said C. G. Lewellyn a written protest, a copy of which protest is attached to and made a part of plaintiff's Statement as Exhibit B.

Eighth. That subsequently the plaintiff filed with the said C. G. Lewellyn for presentation to the Commissioner of Internal Revenue a claim for the refund of the net amount of the assessment of said income tax, to wit: $114,034.34, and also the amount of the credit allowed thereon of $210.06, representing an over assessment against the corporation on the basis of its return as originally filed, the two amounts constituting the entire amount of the additional assessment in the sum of $114,244.40. A copy of the said claim for refund is attached to and a part of plaintiff's Statement as Exhibit C.

Ninth. That after consideration of said claim for refund,
64 the Commissioner of Internal Revenue rejected the same, and the said C. G. Lewellyn was instructed to notify the Gulf Oil Corporation, and on or about April 13, 1915, did so notify said corporation, that said claim was rejected, a copy of which notice is attached to and made a part of plaintiff's statement as Exhibit D.

Tenth. The plaintiff is a holding company, and continuously since its organization in February, 1907, it has been the owner of all of the capital stock of the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company, the Gulf Pipe Line Company of Oklahoma, and for many years has been the owner of all of the capital stock of the Indiana Oil and Gas Company and the Gulf Commissary Company, except in the case of each company of directors' qualifying shares, and was the owner of said shares during all of the period in which the earnings have accumulated out of which the dividends in question in this case were declared and paid.

That with the exception of the Indiana Oil and Gas Company and the Gulf Commissary Company, and a dividend of the J. M. Guffey Petroleum Company hereafter referred to, no dividends were paid by any of the above-named subsidiary companies prior to December 31, 1912. All of the earnings of said companies prior to

said date were either invested as earned in the extension and development of the properties and business of the companies mentioned or allowed to accumulate in the treasuries of such companies respectively, and all of the said earnings were actually used and required in carrying on the business of the subsidiary companies.

In January of 1913, the officers of the Gulf Oil Corpora-
65 tion, plaintiff, decided that the accumulated earnings and surpluses of these subsidiary companies should be taken over by the plaintiff company in the form of dividends and accordingly:

Eleventh. On February 7, 1913, the J. M. Guffey Petroleum Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $3,749,750.00. Payment of said dividend was made April 11, 1913.

Twelfth. On February 7, 1913, the Gulf Pipe Line Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $4,724,055.00. Payment of said dividend was made April 11, 1913.

Thirteenth. On February 7, 1913, the Gulf Pipe Line Company of Oklahoma declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $2,597,660.00. Payment of said dividend was made April 11, 1913.

Fourteenth. On January 8, 1913, the Indiana Oil and Gas Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $338,000.00; and on February 24, 1913, declared and authorized the immediate payment of a dividend, of which the Gulf Oil Corporation received $10,-
66 000.00. Payment of the dividend declared January 8, 1913, was made on that day and payment of the dividend declared February 24, 1913, was made on February 25, 1913.

Fifteenth. On December 17, 1912, the Gulf Commissary Company declared and authorized out of its accumulated surplus earned prior to December 17, 1912, the payment of a dividend, of which the Gulf Oil Corporation received $4,975.00. Payment of said dividend was not made until January 4, 1913.

Sixteenth. Payment of said dividends by the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company and the Gulf Pipe Line Company of Oklahoma was made as follows:

The several companies mentioned, together with certain other companies, constituted a single enterprise carried on by the plaintiff, that enterprise consisting in a general way of the production and purchase of crude oil, the transportation of oil and the refining and marketing thereof. During the period in question the business of producing and purchasing oil was carried on principally in the State of Oklahoma, where also the oil was gathered and stored; the transportation of oil by pipe lines from points in the State of Oklahoma and in Texas to the Gulf of Mexico, where the Company owned refineries in which the refined products were manufactured. The

marketing of these products was carried on over a large part of the United States and in foreign countries, and for the purpose of shipping such refined products the Company owned and operated its own fleet of carrying vessels.

At the time of the declaration of the dividends before referred to all of the earnings of the subsidiary companies had been re-
67 tained in those companies, treating the subsidiary companies collectively, although for the purposes of the enterprise as a whole it was necessary that the funds or credit of one subsidiary be loaned to and used by another. As a result of this at the time of the declaration of said dividends there existed among the subsidiary companies considerable indebtedness, evidenced by book accounts, such indebtedness arising almost entirely through transactions between such companies in the purchase and sale of oil or property.

All of these funds were either invested in properties or actually required in the carrying on of the business of the subsidiary companies, so that the subsidiary companies were without moneys with which to make payment of this inter-company indebtedness. For the purpose of clearing the transaction the matter was consummated on the same day, to wit: April 11, 1913, and in this way:

The Gulf Oil Corporation took over upon its books the amount of the dividends before mentioned (other than the Indiana Oil and Gas Company and the Gulf Commissary Company, which it had already received) and at the same time set up upon its books accounts receivable owing to it by various subsidiaries aggregating the amount of the dividends so received. Upon the books of the subsidiary companies entries showing the same facts were made, and all of these entries were made upon vouchers passed between the parties to the transactions.

As a result, the subsidiary companies collectively, after the payment of this dividend, owned substantially the same amount as prior thereto had been owing to some of the subsidiaries by other
68 subsidiaries, but such indebtedness was shifted so that it was owing entirely to the Gulf Oil Corporation; and the Gulf Oil Corporation, after the payment of the dividends, had no property or assets which prior thereto was not represented in the shares of stock of the subsidiary companies owned by it, but it had upon its books accounts receivable of subsidiary companies which together with the shares of stock of the various subsidiary companies owned by it represented the same property and assets as was represented by the shares of stock alone prior to the declaration and payment of said dividends.

Seventeenth. The only dividend declared by the J. M. Guffey Petroleum Company prior to January 1st, 1913, was a dividend of $2,024,865.00, declared and paid in the year 1912, but the moneys out of which that dividend was paid arose out of the sale by the J. M. Guffey Petroleum Company to the Gulf Refining Company (another subsidiary of the plaintiff company) of certain ships owned by it and was merely the carrying out of a change of ownership of the property from one subsidiary to another.

Eighteenth. That the said J. M. Guffey Petroleum Company, Gulf

Pipe Line Company, Gulf Pipe Line Company of Oklahoma, Indiana Oil and Gas Company and Gulf Commissary Company were all corporations subject to the payment of the Excise Tax imposed by the Act of Congress of August 5, 1909, and that all of said companies had in fact paid all of the taxes imposed upon them under the provisions of the said Act, including such taxes on the earnings from which said dividends were declared.

69 *Request for Conclusion of Law.*

The Court is respectfully requested to make the following conclusion of law, viz:

That the dividends declared and paid as aforesaid to the Gulf Oil Corporation were not subject to the tax imposed and collected, and the plaintiff is entitled to recover judgment in this case in the sum of $114,244.40, with interest from February 17, 1915.

REED, SMITH, SHAW & BEAL,
Attorneys for Plaintiff.

70 *Opinion of the Court.*

Filed March 12, 1917.

ORR, *J.*:

The plaintiff has brought this suit to recover from the defendant the sum of $114,244.40 with interest from February 17, 1915; the payment of which was illegally exacted of the plaintiff by reason of a wrong construction of certain provisions of the Act of Congress of October 3, 1913, 38 Stat., 114-166, commonly called "The Income Tax Law of 1913." In pursuance of a stipulation in writing, the case has been tried by the court without a jury.

From the evidence produced at the trial, the Court has found the following

Facts.

First. The Gulf Oil Corporation is a corporation duly organized under the laws of the State of New Jersey. C. G. Lewellyn is the Collector of Internal Revenue for the Twenty-third District of Pennsylvania, being duly commissioned as such pursuant to the laws of the United States of America.

Second. The Gulf Oil Corporation, on the 14th day of February, 1914, in compliance with the provisions of the Act of Congress of October 3, 1913, made a return of its annual net income for the twelve months ending December 31, 1913, as required by said Act. In making said return the Gulf Oil Corporation certified that it had not included in the statement of gross income for the year
71 1913 certain dividends amounting to $11,424,440.00 received by it from subsidiary companies out of earnings and surplus of said subsidiary companies accrued prior to January 1, 1913.

Third. In said return the Gulf Oil Corporation showed net income for the twelve months ending December 31, 1913, of $886,250.44, but under date of May 1, 1914, the said C. G. Lewellyn, Collector, mailed to said corporation notice of an assessment of tax thereon amounting to $9,072.56. A claim for abatement of this overcharge, amounting to $210.06, was filed with the Collector June 9, 1914, and on June 30, 1914, the Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, the sum of $8,862.50, being the amount of said assessment, less the $210.06 for which abatement was claimed. Said claim for abatement having been disallowed, said Gulf Oil Corporation, on the 5th day of November, 1914, paid the said Collector the additional sum of $210.06, with interest amounting to $6.30, making a total payment of $216.36.

Fourth. On the 30th day of December, 1914, the said C. G. Lewellyn, Collector, acting under instructions from the Commissioner of Internal Revenue at Washington, D. C., mailed notice and demand for tax assessment against the Gulf Oil Corporation for the year ending December 31, 1913, amounting to $114,034.34. In fact, this additional assessment amounted to $114,244.40, being the 1 per cent upon the entire amount of the dividends received by the Gulf Oil Corporation from subsidiary companies out of surplus accrued to such subsidiaries prior to January 1, 1913, and payable to the Gulf Oil Corporation prior to March 1, 1913, and said additional assessment was based solely on said dividends. In making the assessment, however, the Commissioner of Internal Revenue reconsidered
72 and allowed the previous claim or abatement of $210.06, erroneously assessed against the corporation in the original assessment, and credited the same as having been paid upon the assessment of December 30, 1914, leaving the net balance of such assessment $114,034.34 as stated.

Fifth. The notice and demand of the said C. G. Lewellyn, Collector, for the payment of this additional tax recited that if the tax is not paid on or before January 8, 1915, it would be the duty of the Collector to collect said tax, together with 5 per cent additional and interest at the rate of 1 per cent per month until paid.

Sixth. That subsequently the plaintiff filed with the defendant for presentation to the Commissioner of Internal Revenue a claim for the abatement of said income tax amounting to $114,034.34, a copy of which claim is attached to and made a part of plaintiff's Statement as Exhibit A. That after an examination of said claim for abatement the Commissioner of Internal Revenue rejected the same.

Seventh. On February 17, 1915, the said Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, said additional income taxes assessed for the period ending December 31, 1913, in the sum of $114,034.34, and at the same time filed with said C. G. Lewellyn a written protest, a copy of which protest is attached to and made a part of plaintiff's Statement as Exhibit B.

Eighth. That subsequently the plaintiff filed with the said C. G. Lewellyn for presentation to the Commissioner of Internal
73 Revenue a claim for the refund of the net amount of the assessment of said income tax, to wit: $114,034.34, and also

the amount of the credit allowed thereon of $210.06, representing an over assessment against the corporation on the basis of its return as originally filed, the two amounts constituting the entire amount of the additional assessment in the sum of $114,244.40. A copy of the said claim for refund is attached to and a part of plaintiff's statement as Exhibit C.

Ninth. That after consideration of said claim for refund, the Commissioner of Internal Revenue rejected the same, and the said C. G. Lewellyn was instructed to notify the Gulf Oil Corporation, and on or about April 13, 1915, did so notify said corporation, that said claim was rejected, a copy of which notice is attached to and made a part of plaintiff's statement as Exhibit D.

Tenth. The plaintiff is a holding company, and continuously since its organization in February, 1907, it has been the owner of all of the capital stock of the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company, the Gulf Pipe Line Company of Oklahoma, and for many years has been the owner of all of the capital stock of the Indiana Oil and Gas Company and the Gulf Commissary Company, except in the case of each company of directors' qualifying shares, and was the owner of said shares during all of the period in which the earnings have accumulated out of which the dividends in question in this case were declared and paid.

That with the exception of the Indiana Oil and Gas Company and the Gulf Commissary Company, and a dividend of the J. M.
74 Guffey Petroleum Company hereafter referred to, no dividends were paid by any of the above-named subsidiary companies prior to December 31, 1912. All of the earnings of said companies prior to said date were either invested as earned in the extension and development of the properties and business of the companies mentioned or allowed to accumulate in the treasuries of such companies respectively, and all of the said earnings were actually used and required in carrying on the business of the subsidiary companies.

In January of 1913 the officers of the Gulf Oil Corporation, plaintiff, decided that the accumulated earnings and surpluses of these subsidiary companies should be taken over by the plaintiff company in the form of dividends and accordingly:

Eleventh. On February 7, 1913, the J. M. Guffey Petroleum Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $3,749,750. Payment of said dividend was made April 11, 1913.

Twelfth. On February 7, 1913, the Gulf Pipe Line Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $4,724,055.00. Payment of said dividend was made April 11, 1913.

Thirteenth. On Februar 7, 1913, the Gulf Pipe Line Company of Oklahoma declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a
75 dividend, of which the Gulf Oil Corporation received $2,597,660. Payment of said dividend was made April 11, 1913.

Fourteenth. On January 8, 1913, the Indiana Oil and Gas Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $338,000.00; and on February 24, 1913, declared and authorized the immediate payment of a dividend, of which the Gulf Oil Corporation received $10,000.00. Payment of the dividend declared January 8, 1913, was made on that day and payment of the dividend declared February 24, 1913, was made on February 25, 1913.

Fifteenth. On December 17, 1912, the Gulf Commissary Company declared and authorized out of its accumulated surplus earned prior to December 17, 1912, the payment of a dividend, of which the Gulf Oil Corporation received $4,975.00. Payment of said dividend was not made until January 4, 1913.

Sixteenth. Payment of said dividends by the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company and the Gulf Pipe Line Company of Oklahoma was made as follows:

The several companies mentioned, together with certain other companies, constituted a single enterprise carried on by the plaintiff, that enterprise consisting in a general way of the production and purchase of crude oil, the transportation of oil and the refining and marketing thereof. During the period in question the business of
producing and purchasing oil was carried on principally in
76 the State of Oklahoma, where also the oil was gathered and
stored; the transportation of oil by pipe lines from points in the State of Oklahoma and in Texas to the Gulf of Mexico, where the company owned refineries in which the refined products were manufactured. The marketing of these products was carried on over a large part of the United States and in foreign countries, and for the purpose of shipping such refined products the Company owned and operated its own fleet of carrying vessels.

At the time of the declaration of the dividends before referred to all of the earnings of the subsidiary companies had been retained in those companies, treating the subsidiary companies collectively, although for the purposes of the enterprise as a whole it was necessary that the funds or credit of one subsidiary be loaned to and used by another. As a result of this at the time of the declaration of said dividends there existed among the subsidiary companies considerable indebtedness, evidenced by book accounts, such indebtedness arising almost entirely through transactions between such companies in the purchase and sale of oil or property.

All of these funds were either invested in properties or actually required in the carrying on of the business of the subsidiary companies, so that the subsidiary companies were without moneys with which to make payment of this inter-company indebtedness. For the purpose of clearing the transaction the matter was consummated on the same day, to wit: April 11, 1913, and in this way:

The Gulf Oil Corporation took over upon its books the amount of
the dividends before mentioned (other than the Indiana Oil
77 and Gas Company and the Gulf Commissary Company, which
it had already received, and at the same time set up upon its

books accounts receivable owing to it by various subsidiaries aggregating the amount of the dividends so received. Upon the books of the subsidiary companies entries showing the same facts were made, and all of these entries were made upon vouchers passed between the parties to the transactions.

As a result, the subsidiary companies collectively, after the payment of this dividend, owed substantially the same amount as prior thereto had been owing to some of the subsidiaries by other subsidiaries, but such indebtedness was shifted so that it was owing entirely to the Gulf Oil Corporation; and the Gulf Oil Corporation, after the payment of the dividends, had no property assets which prior thereto was not represented in the shares of stock of the subsidiary companies owned by it, but it had upon its books accounts receivable of subsidiary companies which together with the shares of stock of the various subsidiary companies owned by it represented the same property and assets as was represented by the shares of stock alone prior to the declaration and payment of said dividends.

Seventeenth. The only dividend declared by the J. M. Guffey Petroleum Company prior to January 1st, 1913, was a dividend of $2,024,865.00 declared and paid in the year 1912, but the moneys out of which that dividend was paid arose out of the sale by the J. M. Guffey Petroleum Company to the Gulf Refining Company (another subsidiary of the plaintiff company) of certain ships owned by it and was merely the carrying out of a change of ownership of the property from one subsidiary to another.

Eighteenth. That the said J. M. Guffey Petroleum Com-
78 pany, Gulf Pipe Line Company, Gulf Pipe Line Company of Oklahoma, Indiana Oil and Gas Company and Gulf Commissary Company were all corporations subject to the payment of the Excise Tax imposed by the Act of Congress of August 5, 1909, 36 Statutes, 11-112, and that all of said companies had in fact paid all of the taxes imposed upon them under the provisions of the said Act, including such taxes on the earnings from which said dividends were declared.

Discussion.

The payment of all taxes hitherto required of the several subsidiaries by acts of Congress, and the full disclosure by the plaintiff in its return for 1913 of the dividends from subsidiaries negative any suggestion that the conduct of the plaintiff has been in any way evasive or otherwise improper. The plaintiff has merely asserted its legal rights. Its right to bring this action is clear because it has performed all the conditions precedent to suit which the law requires. The chief matter in controversy between the parties is whether the dividends declared by the subsidiaries are within the provisions of the Income Tax Law (Act of October 5, 1913, 38 Stat., 114-172 Section II, G.) Referring to said Law (ibid. p. 166) Section II-A, we find in sub-division 1, a provision for a tax of one per centum "upon the entire net income arising or accruing from all sources in the preceding calendar year, to every citizen of the United States,"

and in sub-division 2, a provision for a tax in addition to the
79 foregoing which is called the "Normal Income Tax" upon the net income of every individual when the same shall exceed the amounts therein specified.

Turning to Section II G of the Act (ibid. p. 172) we find the following language: "That the normal tax hereinbefore imposed upon individuals likewise shall be levied, assessed, and paid annually upon the entire net income arising or accruing from all sources during the preceding calendar year to every corporation" etc., with certain exclusions not necessary to be considered in the present case, because the plaintiff is not within the exclusions or exceptions mentioned. The question, therefore is: are the dividends, which are the subject of the assessment in controversy in this case, being as it appears but distributions of accumulations of profits extending over a long period of years, income within the meaning of the said Income Tax Law? The defendant contends that, so far as the Plaintiff Corporation is concerned, the distribution of such profits and earnings must be considered as part of the net income arising or accruing to it during the year 1913. He urges that the Plaintiff Corporation had no interest in or title to any of the earnings of the subsidiaries until after such dividends were declared by them, and has cited many authorities holding that shareholders in a corporation do not have any enforceable title to profits of corporations until dividends are actually declared by the directors of such corporations. It is unnecessary to consider these cases in detail because they do not control the question now before the Court. It is preferable to adopt the language of Mr. Justice Clifford in The Collector vs. Hubbard, 79 U. S. 1-18. A case not otherwise helpful.

"Decided cases are referred to, in which it is held that a
80 stockholder has no title for certain purposes to the earnings, net or otherwise, of a railroad prior to the dividend being declared, and it cannot be doubted that those decisions are correct as applied to the respective subject'-matters involved in the controversies. Grant all that, still it is true that the owner of a share of stock in a corporation holds the share with all its incidents, and that among those incidents is the right to receive all future dividends, that is, his proportional share of all profits not then divided. Profits are incident to the share to which the owner at once becomes entitled provided he remains a member of the corporation until a dividend is made. Regarded as an incident to the shares, undivided profits are property of the shareholder, and as such are the proper subject of sale, gift or devise. Undivided profits invested in real estate, machinery, or raw material for the purpose of being manufactured are investments in which the stockholders are interested, and when such profits are actually appropriated to the payment of the debts of the corporation they serve to increase the market value of the shares, whether held by the original subscribers or by assignees."

While decisions bearing upon the right to stock dividends declared by corporations in distribution of accumulated earnings may not be specially helpful, we find very careful consideration of such ques-

tions in Gibbons vs. Mahon, 136 U. S. 549, and on page 558 the following language by Mr. Justice Gray is found:

"Reserved and accumulated earnings, so long as they are held and invested by the corporation, being part of its corporate property, it follows that the interest therein, represented by each share,
81 is capital, and not income, of that share, as between the tenant for life and the remainderman, legal or equitable, thereof."

The case of Bailey vs. Railroad Company, 106 U. S. 109 is of value in the consideration of the question now before the Court. That case, in the lower Court, was a proceeding by the Railroad Company to recover from Bailey, a Collector of Internal Revenue, moneys claimed by the Railroad Company to be illegally exacted as Income Tax within the meaning of Section 122 of an Act of Congress passed in 1864, 13 Stat., 223-284. The Act provided that certain corporations should be subject to and pay a tax on the amount of interest etc., and upon "any dividend in scrip or money due or payable to its stockholders as part of the earnings, profits, income or gain of such Company and all profits of such company carried to the account of any fund or used for construction." The Government had undertaken to assess an income tax under that Act of 1864 upon a scrip dividend made in 1868 distributing earnings which had accrued through the period from 1853 to 1868. The Court held that there was no authority for the imposition of the tax upon so much of the earnings as accrued prior to 1862, the date from which the tax took effect. It was argued on behalf of the plaintiff in error representing the Government that by the express terms of the Act, inasmuch as the certificates issued to the stockholders evidencing their proportions in the scrip dividend "being a declaration of a dividend as part of the earnings, profits, income, or gains of the company, are taxable upon the amount thereof without deduction; that the policy as well as the language of the act fixes the charge upon the declaration itself when made effectual as between the company and its stockholders, and, for the purposes of taxation, concludes both as to the amount subject to the tax; and that the rule is reasonable as
82 furnishing an obvious standard and the only safe criterion for the assessment of the tax to prevent fraudulent evasions. And consequently that when such a dividend has once been declared, and ascertained to come within the description of the law as a subject of taxation, all of the rest follows, and the amount declared is necessarily established as the amount to be taxed."

The foregoing quotation is the statement of the contention on the part of the Government as it appears in the opinion of Mr. Justice Matthews (p. 114). The learned justice proceeds as follows:

"The soundness of this mode of interpretation, and its application to ordinary cases, may well be admitted; but it cannot be applied to every case without a careful regard to its necessary limitations.

It should be borne in mind, in the first place, that the tax provided for in this section is an annual income tax, and its subject is the interest paid and profits earned by the company for each year, and year by year; and that both by the express letter of the law, and its

necessary implications, the tax is not laid on any of these funds which came into being before the time prescribed in the act. And in the ordinary execution of the law, it was contemplated that the funds to be taxed, and the tax imposed upon them, would be concurrent, as to each fiscal year; the scheme of the statute being to levy the tax upon the income for the year ending on the 31st of December next preceding the assessment; and while it would be altogether admissable to go back, for the purpose of assessing a tax upon a proper fund which had accrued during a previous year and
83 escaped taxation, nevertheless the tax imposed would be for the omitted year. But no tax, in contemplation of the law, accrued upon the fund, except for the year in which the fund itself accrued."

The foregoing seems to be a direct authority in support of the contention of the plaintiff in the present case, for the language of the Act of 1913 is no clearer in showing an intent of the law makers to tax earnings accrued prior to the time they were subjected to the operation of the Act than was the language of the Act of 1864. The argument that there should be a different construction of the Act of 1913 from that given to the Act of 1864 is weakened by the fact that at the time the earnings in the present case accrued, the authority given to Congress by the Sixteenth Amendment was wanting. It seems to be perfectly clear that the advances in the value of property during a series of years can, in no proper sense be considered gains, profits *of* income of any one particular year of the series, although the entire amount of the advance may be at one time turned into money by the sale of the property (See Gray vs. Darlington, 82 U. S. 63, and Gauley Mountain Coal Company vs. Hays, 230 Fed. 110.)

The Income Tax Law of 1913 has already received the consideration of the Federal Courts. Indeed, the very contention of the plaintiff in this case has been supported in the decisions by the Circuit Court of Appeals of the Eighth Circuit in Lynch vs. Turrish, 236 Fed. 653 and Lynch vs. Hornby, 236 Fed. 661. Nothing could add to the reasoning or strengthen the conclusions reached by that Court. A mere statement from the syllabus of the first case is sufficient
84 for present purposes. "The enhanced value of property of a corporation which accrues from the gradual increase in its value during a series of years prior to the effective date of an Income Tax Law, although divided or distributed by dividends or otherwise, subsequent to that date, does not become 'income, gains or profits' taxable under an act, but is rather an 'increase of capital assets.'" The specific facts in each of those cases are not specially material. The complaints of the plaintiffs therein were generally the same as the complaint of the plaintiff in the present case. Each had been assessed and compelled to pay a tax levied upon a distribution of assets, because of the mistaken view of the Collector of Internal Revenue that such distribution of assets was "income, gains or profits within the meaning of the Income Tax Law." The difference between the plaintiffs in those cases and the plaintiff in the present case is that they are individuals while the plaintiff in

the case at bar is a corporation. Such difference, however, is not material, because as has been seen under the law, the income to be taxed is the same in the case of corporations as in the case of individuals. Moreover Section II Par. G, Sub-Division (*b*) provides for the ascertainment of the net income of a corporation by making deductions, not from its gross receipts but from its "gross income."

It is perhaps worthy of observation that Congress being without authority to levy an income tax until February 25, 1913, when the Sixteenth Amendment was adopted, provided in the Act of 1913, Par. G, (*c*) that the tax for that year should be upon the entire net income accrued within that portion of said year from March 1st to December 1st, both dates inclusive, to be ascertained by taking five-sixths of the entire net income for said calendar year. In paragraph
S, which repeals the Excise Tax of 1909, save with respect to
85 pending cases, there is a provision that for the special Excise Tax covering the first two months of 1913, it should be computed upon one-sixth of the entire net income of the corporation for said year, which said income, however, was to be asceretained in accordance with sub-division G of Section II of the Act of 1913. There is a further provision in the Act of 1913, that the Act of 1909 should remain in force for the collection of the Excise Tax in the latter act, but provided that for the year 1913, it should not be necessary to make more than one return and assessment for all the taxes imposed.

Without further referring to other provisions in the repealing portion of the Act of 1913, it seems clear that the Excise Tax for January and February was intended to be computed upon "one-sixth of the entire net income" for the year 1913 and that said net income was to be ascertained in accordance with the provisions of subdivision G, Section II of that Act. The provisions in the repealing part of the Act of 1913 do not change or add to the subject of taxation. That subject of taxation was to be net income accruing to the corporation. Unless the dividends in question are taxable as income under the prior provisions of the Act which related to corporations, then clearly such dividends are not taxable under the proviso.

Because of the view this Court has taken of the rights of the plaintiff in this case, it is not deemed necessary or perhaps even profitable to consider other questions that have been raised. It seems to be clear that the Gulf Oil Corporation, being a holding company and owning all the shares except such as were necessary to qualify
the directors (one share for each) in reality receiving nothing
86 in pursuance of the declaration of dividends by the subsidiaries which it has not owned before.

Under all the facts and in consideration of the law applicable thereto, this Court has reached the following

Conclusions.

1. The dividends in question in this suit were not subject to the tax imposed, because they were a distribution of surplus earnings arising through a period of years and which had accrued to, and the equitable ownership thereof was vested in, the plaintiff prior to

January 1, 1913, and such earnings were not intended by Congress to be subject to taxation.

2. That judgment should be entered in favor of the plaintiff and against the defendant for the amount claimed, to-wit: $114,244.40 with interest, to be added from February 17, 1915, and that an order for judgment, with a correct calculation of the debt and interest may be submitted.

87 *Order and Exception.*

Filed March 17, 1917.

And now, to wit, March 17th, 1917, upon motion of Counsel for plaintiff, the Clerk of this Court is ordered and directed to enter judgment for the Gulf Oil Corporation, plaintiff, and against C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, defendant, in the sum of one hundred twenty-eight thousand five hundred twenty-four and 95-100 Dollars ($128,524.95), liquidated as follows:

Amount of claim	$114,244.40
Interest from February 17, 1915, to March 17, 1917	14,280.55
Amount of judgment	$128,524.95

PER CURIAM.

Eo die, Counsel for the Defendant excepts to the foregoing action of the Court and at his instance exception noted and bill sealed.

CHAS. P. ORR,
United States District Judge.

88 *Judgment.*

March 17th, 1917, pursuant to Order of Court, judgment is hereby entered in favor of Gulf Oil Corporation and against C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, in the sum of One Hunded Twenty-eight Thousand Five Hundred Twenty-four and 95-100 ($128,524.95) Dollars.

J. WOOD CLARK, *Clerk.*

Assignments of Error.

Filed April 14, 1917.

And now, April 14, 1917, comes the above-named defendant by E. Lowry Humes, United States Attorney for the Western District of Pennsylvania, and in connection with the petition for Writ of Error makes the following Assignments of Error:

First. The Court erred in the following Finding of Fact:

"The several companies mentioned, together with certain other companies, constituted a single enterprise carried on by the plaintiff, that enterprise consisting in a general way of the production and purchase of crude oil, the transportation of oil and the refining and
89 marketing thereof. During the period in question the business of producing and purchasing oil was carried on principally in the State of Oklahoma, where also the oil was gathered and stored; the transportation of oil by pipe lines from points in the State of Oklahoma and in Texas to the Gulf of Mexico, where the company owned refineries in which the refined products were manufactured. The marketing of these products was carried on over a large part of the United States and in foreign countries, and for the purpose of shipping such refined products the company owned and operated its own fleet of carrying vessels."

Second. The Court erred in using the following language in the opinion which it filed, to wit:

"The Income Tax Law of 1913 has already received the consideration of the Federal Courts. Indeed, the very contention of the plaintiff in this case has been supported in the decisions by the Circuit Court of Appeals of the Eighth Circuit in Lynch vs. Turrish, 236 Fed. 653 and Lynch vs. Hornby, 236 Fed. 661. Nothing could add to the reasoning or strengthen the conclusions reached by that Court."

Third. The Court erred in using the following language in the opinion:

"Without further referring to other provisions in the repealing portion of the Act of 1913, it seems clear that the Excise Tax for January and February was intended to be computed upon 'one-sixth of the entire net income' for the year 1913 and that said net income was to be ascertained in accordance with the pro-
90 visions of sub-division G, Section II of that Act. The provisions in the repealing part of the Act of 1913 do not change or add to the subject of taxation. That subject of taxation was to be net income accruing to the corporation. Unless the dividends in question are taxable as income under the prior provisions of the Act which related to corporations, then clearly such dividends are not taxable under the proviso."

Fourth. The Court erred in using the following language in the opinion:

"It seems to be clear that the Gulf Oil Corporation, being a holding company and owning all the shares except such as were necessary to qualify the directors (one share for each) in reality receiving nothing in pursuance of the declaration of dividends by the subsidiaries which it has not owned before."

Fifth. The Court erred in using the following language in the opinion:

"The dividends in question in this suit were not subject to the tax imposed, because they were a distribution of surplus earnings arising through a period of years and which had accrued to, and the equitable ownership thereof was vested in, the plaintiff prior to

January 1, 1913, and such earnings were not intended by Congress to be subject to taxation."

Sixth. The Court erred in using the following language in the opinion:

91 "That judgment should be entered in favor of the plaintiff and against the defendant for the amount claimed, to wit: $114,244.40 with interest, to be added from February 17, 1915, and that an order for judgment, with a correct calculation of the debt and interest may be submitted."

Seventh. The Court erred in making the following order, to wit:

"And now, to wit, March 17th, 1917, upon motion of Counsel for plaintiff, the Clerk of this Court is ordered and directed to enter judgment for the Gulf Oil Corporation, plaintiff, and against C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, defendant, in the sum of One Hundred Twenty-eight Thoursand Five Hundred and Twenty-four and 95/100 Dollars ($128,524.95), liquidated as follows:

Amount of claim	$114,244.40
Interest from February 17, 1915, to March 17, 1917	14,280.55
Amount of judgment	$128,524.95

PER CURIAM."

E. LOWRY HUMES,
United States Attorney and
Attorney for Plaintiff in Error.

92 *Petition for a Writ of Error.*

Filed April 14, 1917.

To the Honorable Charles P. Orr, Judge of the United States District Court for the Western District of Pennsylvania:

C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, defendant in this case, by his attorney, E. Lowry Humes, United States Attorney for the Western District of Pennsylvania, considering himself aggrieved by the rulings and decisions of the Court in the above entitled cause, and by judgment thereon, hereby makes application for a Writ of Error to the United States Circuit Court of Appeals for the Third Circuit in order that the said Circuit Court of Appeals may review the action of the Court below, and prays that a Writ of Error may be allowed; that a transcript of the record, proceedings and papers in said cause, duly authenticated, may be sent to the said Circuit Court of Appeals, as the law in such cases provides.

E. LOWRY HUMES,
United States Attorney and
Attorney for the Plaintiff in Error.

Order.

And now, to wit, April 14, 1917, on presentation of the foregoing petition and on motion of E. Lowry Humes, United States Attorney, a Writ of Error is hereby granted the defendant to the United States Circuit Court of Appeals for the Third Circuit as prayed for.

CHARLES P. ORR,
U. S. District Judge.

93 *Bill of Exceptions.*

Filed April 23, 1917.

Be it remembered, at the above number and term, came into this Court, the Gulf Oil Corporation, a corporation organized and existing under the laws of the State of New Jersey, plaintiff, and filed its statement of claim against C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, defendant (see Statement of Claim), and the said defendant filed his Affidavit of Defense to said statement (see Affidavit of Defense); and thereupon issue was duly joined and afterwards, to wit, at a session of this Court, held on the 30th day of January, A. D. 1917, the said issue came on to be tried before Honorable Charles P. Orr, District Judge, without a jury (see Waiver of Jury Trial), at which time appeared the plaintiff and defendant by their respective attorneys, whereupon the witness whose name is set forth in the testimony—which testimony is made a part of this Bill of Exceptions, (see testimony)—was called and duly sworn and testified as in said testimony set forth; and on the 30th day of January, 1917, the plaintiff filed request for Findings of Fact and Conclusions of Law (see Request for Findings of Fact and Conclusions of Law); and on the 12th day of March, 1917, the Court filed its opinion and Findings of Fact and Conclusions of Law in favor of the plaintiff (see Opinion of Court), and on the 17th day of March, 1917, the Court ordered and directed the Clerk of this Court to enter judgment for the Gulf Oil Corporation, plaintiff, against C. G. Lewellyn, Collector of Internal Revenue, in the sum of One Hundred and Twenty-eight Thousand Five Hundred and
94 Twenty-four Dollars and Ninety-five cents ($128,524.95), (See Order) and counsel for the defendant excepted to the said order of the Court (see Exceptions), which exception was duly noted and bill sealed.

Whereupon, on the 14th day of April, 1917, the said defendant filed his petition for a writ of error and presented said petition, with his Assignment of Errors, and on the same day said writ was duly allowed and issued, and a citation was thereupon issued and served on counsel for the plaintiff, and thereupon the aforesaid Judge did to this Bill of Exceptions, in pursuance of the request

of Plaintiff in Error, and of the law, put his seal this 23rd day of April, A. D., 1917.

CHAS. P. ORR, [SEAL.]
Judge for the United States District Court for the Western District of Pennsylvania.

The foregoing Bill of Exceptions presented to us and found correct.

REED, SMITH, SHAW & BEAL,
Attorneys for Plaintiff,
By W. A. SEIFERT.

95 *Certificate.*

WESTERN DISTRICT OF PENNSYLVANIA, *ss:*

I, J. Wood Clark, Clerk of the District Court of the United States, for the Western District of Pennsylvania, do hereby certify that the annexed and foregoing pages contain a true and correct copy of the record of proceedings ordered to be printed in the above entitled case, so full and entire as the same remains of record and on file in my office, in the City of Pittsburgh, in said District.

In testimony whereof, I have hereunto signed my name and affixed the seal of the said Court, at Pittsburgh, this — day of May, A. D. 1917.

—— ——, *Clerk.*

96 In the United States Circuit Court of Appeals for the Third Circuit, March Term, 1917.

No. 2254.

C. G. LEWELLYN, Collector of Internal Revenue, Plaintiff in Error,

vs.

GULF OIL CORPORATION, Defendant in Error.

And afterwards, to wit, on the 26th day of June, 1917, come the parties aforesaid by their counsel aforesaid, and this case being called for argument sur pleadings and briefs, before the Hon. Joseph Buffington, Hon. John B. McPherson and Hon. Victor B. Woolley, Circuit Judges, and the Court not being fully advised in the premises, takes further time for the consideration thereof.

And afterwards, to wit, on the eighth day of October, 1917, come the parties aforesaid by their counsel aforesaid, and the Court now being fully advised in the premises, renders the following decision

97 In the United States Circuit Court of Appeals for the Third Circuit, March Term, 1917.

No. 2254.

LEWELLYN, Collector,

vs.

GULF OIL CORPORATION, Plaintiff Below.

Error to the District Court of the United States for the Western District of Pennsylvania.

Before Buffington, McPherson, and Woolley, Circuit Judges.

McPHERSON, *C. J.*:

In this suit the Gulf Oil Corporation seeks to recover the taxes for 1913 that were assessed against it under the Act of Oct. 3, 1913. Payment was made under protest, and repayment was refused by the Commissioner of Internal Revenue. The Corporation recovered a judgment of $128,524.95: 242 Fed. 709.

The trial was without a jury, and for convenience we repeat here the findings of fact in the district court:

98 1. The Gulf Oil Corporation is a corporation duly organized under the laws of the State of New Jersey. C. G. Lewellyn is the collector of Internal Revenue for the Twenty-third District of Pennsylvania, being duly commissioned as such pursuant to the laws of the United States of America.

2. The Gulf Oil Corporation, on the 14th day of February, 1914, in compliance with the provisions of the Act of Congress of October 3, 1913, made a return of its annual net income for the twelve months ending December 31, 1913, as required by said Act. In making said return the Gulf Oil Corporation certified that it had not included in the statement of gross income for the year 1913 certain dividends amounting to $11,424,440.00 received by it from subsidiary companies out of earnings and surplus of said subsidiary companies accrued prior to January 1, 1913.

3. In said return the Gulf Oil Corporation showed net income for the twelve months ending December 31, 1913, of $886,250.44, but under date of May 1, 1914, the said C. G. Lewellyn, Collector, mailed to said corporation notice of an assessment of tax thereon amounting to $9,072.56. A claim for abatement of this overcharge, amounting to $210.06, was filed with the Collector June 9, 1914, and on June 30, 1914, the Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, the sum of $8,862.50, being the amount of said assessment, less the $210.06 for which abatement was claimed. Said claim for abatement having been disallowed, said Gulf Oil Corporation, on the 5th day of November, 1914, paid the said Col-

lector the additional sum of $210.06, with interest amounting to $6.30, making a total payment of $216.36.

4. On the 30th day of December, 1914, the said C. G. Lewellyn, Collector, acting under instructions from the Commissioner of Internal Revenue at Washington, D. C., mailed notice and demand for tax assessment against the Gulf Oil Corporation for the year ending December 31, 1913, amounting to $114,034.34. In fact, this additional assessment amounted to $114,244.40, being the 1 per cent upon the entire amount of the dividends received by the Gulf Oil Corporation from subsidiary companies out of surplus accrued to such subsidiaries prior to January 1, 1913, and payable to the Gulf Oil Corporation prior to March 1, 1913, and said additional assessment was based solely on said dividends. In making the assessment, however, the Commissioner of Internal Revenue reconsidered and allowed the previous claim or abatement of $210.06, erroneously assessed against the corporation in the original assessment, and credited the same as having been paid upon the assessment of December 30, 1914, leaving the net balance of such assessment $114,034.34 as stated.

5. The notice and demand of the said C. G. Lewellyn, Collector, for the payment of this additional tax recited that if the tax is not paid on or before January 8, 1915, it would be the duty of the Collector to collect said tax, together with 5 per cent additional and interest at the rate of 1 per cent per month until paid.

6. That subsequently the plaintiff filed with the defendant for presentation to the Commissioner of Internal Revenue a claim for the abatement of said income tax amounting to $114,034.34, a copy of which claim is attached to and made a part of plaintiff's Statement as Exhibit A. That after an examination of said claim for abatement the Commissioner of Internal Revenue rejected the same.

7. On February 17, 1915, the said Gulf Oil Corporation paid to the said C. G. Lewellyn, Collector, said additional income taxes assessed for the period ending December 31, 1913, in the sum of $114,034.34, and at the same time filed with said C. G. Lewellyn a written protest, a copy of which protest is attached to and made a part of plaintiff's Statement as Exhibit B.

99 8. That subsequently the plaintiff filed with the said C. G. Lewellyn for presentation to the Commissioner of Internal Revenue a claim for the refund of the net amount of the assessment of said income tax, to wit: $114,034.34, and also the amount of the credit allowed thereon of $210.06, representing an over assessment against the corporation on the basis of its return as originally filed, the two amounts constituting the entire amount of the additional assessment in the sum of $114,244.40. A copy of the said claim for refund is attached to and a part of plaintiff's statement as Exhibit C.

9. That after consideration of said claim for refund, the Commissioner of Internal Revenue rejected the same, and the said C. G. Lewellyn, was instructed to notify the Gulf Oil Corporation, and on or about April 13, 1915, did so notify said corporation, that said claim was rejected, a copy of which notice is attached to and made a part of plaintiff's statement as Exhibit D.

10. That plaintiff is a holding company, and continuously since its organization in February, 1907, it has been the owner of all of the capital stock of the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company, the Gulf Pipe Line Company of Oklahoma, and for many years has been the owner of all of the capital stock of the Indiana Oil and Gas Company and the Gulf Commissary Company, except in the case of each company of directors' qualifying shares, and was the owner of said shares during all of the period in which the earnings have accumulated out of which the dividends in question in this case were declared and paid.

That with the exception of the Indiana Oil and Gas Company and the Gulf Commissary Company, and a dividend of the J. M. Guffey Petroleum Company hereafter referred to, no dividends were paid by any of the above-named subsidiary companies prior to December 31, 1912. All of the earnings of said companies prior to said date were either invested as earned in the extension and development of the properties and business of the companies mentioned or allowed to accumulate in the treasuries of such companies respectively, and all of the said earnings were actually used and required in carrying on the business of the subsidiary companies.

In January of 1913 the officers of the Gulf Oil Corporation, plaintiff, decided that the accumulated earnings and surpluses of these subsidiary companies should be taken over by the plaintiff company in the form of dividends and accordingly:

11. On February 7, 1913, the J. M. Guffey Petroleum Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend of which the Gulf Oil Corporation received $3,749,750. Payment of said dividend was made April 11, 1913.

12. On February 7, 1913, the Gulf Pipe Line Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $4,724,055.00. Payment of said dividend was made April 11, 1913.

13. On February 7, 1913, the Gulf Pipe Line Company of Oklahoma declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend of which the Gulf Oil Corporation received $2,597,660. Payment of said dividend was made April 11, 1913.

14. On January 8, 1913, the Indiana Oil and Gas Company declared and authorized out of its accumulated surplus earned prior to January 1, 1913, the immediate payment of a dividend, of which the Gulf Oil Corporation received $338,000.00; and on February 24, 1913, declared and authorized the immediate payment of a
100 dividend, of which the Gulf Oil Corporation received $10,000.00. Payment of the dividend declared January 8, 1913, was made on that day and payment of the dividend declared February 24, 1913, was made on February 25, 1913.

15. On December 17, 1912, the Gulf Commissary Company declared and authorized out of its accumulated surplus earned prior to

December 17, 1912, the payment of a dividend, of which the Gulf Oil Corporation received $4,975.00. Payment of said dividend was not made until January 4, 1913.

16. Payment of said dividends by the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company and the Gulp Pipe Line Company of Oklahoma was made as follows:

The several companies mentioned, together with certain other companies, constituted a single enterprise carried on by the plaintiff, that enterprise consisting in a general way of the production and purchase of crude oil, the transportation of oil and the refining and marketing thereof. During the period in question the business of producing and purchasing oil was carried on principally in the State of Oklahoma, where also the oil was gathered and stored; the transportation of oil by pipe lines from points in the State of Oklahoma and in Texas to the Gulf of Mexico, where the Company owned refineries in which the refined products were manufactured. The marketing of these products was carried on over a large part of the United States and in foreign countries, and for the purpose of shipping such refined products the Company owned and operated its own fleet of carrying vessels.

At the time of the declaration of the dividends before referred to all of the earnings of the subsidiary companies had been retained in those companies, treating the subsidiary company collectively, altho for the purposes of the enterprise as a whole, it was necessary that the funds or credit of one subsidiary be loaned to and used by another. As a result of this at the time of the declaration of said dividends there existed among the subsidiary companies considerable indebtedness, evidenced by book accounts, such indebtedness arising almost entirely through transactions between such companies in the purchase and sale of oil or property.

All of these funds were either invested in properties or actually required in the carrying on of the business of the subsidiary companies, so that the subsidiary companies were without moneys with which to make payment of this inter-company indebtedness. For the purpose of clearing the transaction the matter was consummated on the same day, to wit: April 11, 1913, and in this way:

The Gulf Oil Corporation took over upon its books the amount of the dividends before mentioned (other than the Indiana Oil and Gas Company and the Gulf Commissary Company, which it had already received) and at the same time set up upon its books accounts receivable owing to it by various subsidiaries aggregating the amount of the dividends so received. Upon the books of the subsidiary companies entries showing the same facts were made, and all of these entries were made upon vouchers passed between the parties to the transactions.

As a result, the subsidiary companies collectively, after the payment of this dividend, owned substantially the same amount as prior thereto had been owing to some of the subsidiaries by other subsidiaries, but such indebtedness was shifted so that it was owing entirely to the Gulf Oil Corporation; and the Gulf Oil Corporation, after the

payment of the dividends, had no property assets which prior thereto was not represented in the shares of stock of the subsidiary companies owned by it, but it had upon its books accounts receiv-
101 able of subsidiary companies which together with the shares of stock of the various subsidiary companies owned by it represented the same property and assets as was represented by the shares of stock alone prior to the declaration and payment of said dividends.

17. The only dividend declared by the J. M. Guffey Petroleum Company prior to January 1, 1913, was a dividend of $2,024,865.00 declared and paid in the year 1912, but the moneys out of which that dividend was paid arose out of the sale by the J. M. Guffey Petroleum Company to the Gulf Refining Company (another subsidiary of the plaintiff company) of certain ships owned by it and was merely the carrying out of a change of ownership of the property from one subsidiary to another.

18. That the said J. M. Guffey Petroleum Company, Gulf Pipe Line Company, Gulf Pipe Line Company of Oklahoma, Indiana Oil and Gas Company and Gulf Commissary Company were all corporations subject to the payment of the Excise Tax imposed by the Act of Congress of August 5, 1909, 36 Statutes, 11-112, and that all of said companies had in fact paid all of the taxes imposed upon them under the provisions of the said Act, including such taxes on the earnings from which said dividends were declared."

We may summarize the facts as follows: For a number of years the Corporation has owned all the stock (except directors' shares) of the 5 subsidiaries named; and it owned this stock while the subsidiaries were accumulating the earnings that were afterward transferred to the Corporation in the form of dividends. With exceptions not now material, none of the subsidiaries had declared a dividend before December 31, 1912; the previous earnings had been used from time to time in carrying on, extending, and developing, the several enterprises in which they were engaged, and the earnings were properly employed for these purposes. In January 1913 the Corporation decided to have these earnings transferred to itself, and thereupon the subsidiaries took the following steps: On February 7, 1913, the Guffey Petroleum Company, the Gulf Pipe Line Co., and the Gulf Pipe Line Co. of Oklahoma, each declared a dividend, payable immediately, out of the surplus and earnings that had accumulated before January 1, 1913: and on April 11, the Corporation received on this account from the Guffey Co., $3,749,750; from the Gulf Pipe Line Company, $4,724,055; and from the Gulf Pipe Line Company of Oklahoma, $2,597,660. The Indiana Oil and Gas
102 Company declared 2 dividends out of similar surplus and earnings, one on January 8, 1913, from which the Corporation received on the same day $338,000; and one on February 24, 1913, from which on February 25 the Corporation received $10,000. Out of similar earnings and surplus, the Gulf Commissary Company declared a dividend on December 17, 1912, from which on January 4, 1913, the Corporation received $4,975. The respective dividends

were not declared in cash; the earnings, as and when produced, had been employed in the several enterprises, and had thus been invested in different kinds of property. They had not always been used to promote the particular business that had earned them, but had been sometimes used to aid another branch, the subsidiaries keeping a debtor and creditor account among themselves. In this situation, the Corporation made a return to the government of its income for 1913, certifying that the return did not include the dividends referred to, and giving as a reason that they had been declared and paid out of earnings and surplus that had accrued before January 1, 1913. The Collector, however, demanded a total tax of $114,244.40 from the Corporation for the year 1913, basing the assessment solely on the receipt of these dividends. This was in part a franchise tax, and in part an income tax. After various proceedings—claim for abatement, protest, payment, petition for repayment, and the Commissioner's refusal—the controversy reached the district court in the suit now before us. The subsidiaries had all been subject to the excise or franchise tax under the Act of August 5, 1909, and they had all paid the amounts imposed thereunder. The sum in dispute was not charged against the subsidiaries, but against the Corporation alone, and is made up of a franchise tax for the first two months of 1913, and of an income tax for the remaining ten months. The opinion of the district judge sets forth the argument that led him to decide that the taxes were unlawfully imposed—the position
103 being, that the dividends had been declared out of surplus earnings that had accumulated during several years and had accrued to the Corporation (at least in equitable ownership) before January 1, 1913. We are unable to assent to this proposition for the following reasons:

It is first to be observed (and this should be borne distinctly in mind) that the government's levy was not upon the subsidiaries, but upon one of their stockholders, namely, upon the Gulf Oil Corporation. We do not understand the Corporation to lay stress upon a supposed identity of the five subsidiaries with itself, but in any event the facts in proof would furnish a sufficient answer to such a position. No doubt all the companies are engaged together in a common enterprise, but the enterprise has several branches, and each subsidiary attends to its own branch, while the Corporation does the like. Perhaps the Corporation may be more accurately described as uniting and regulating its subsidiaries, but each of the companies, whether holding or subsidiary, is a distinct entity, and is to be so treated. The several companies are not in such relations to each other that the property and obligations and liabilities of one can be regarded as the property and obligations and liabilities of any other. Each owns its own assets, carries on its own business, owes its own debts, pays its own taxes, and enjoys its own income. Under the Excise Act of 1909, each was separately taxed in respect of its own business, and under that Act the Corporation certainly did not include in its own return the proceeds of the business done by the subsidiaries.

Now, if the Corporation had been an individual, and had received

the property in question by the method of transfer described in the findings of fact, the contention would hardly be made that no dividend had in fact been declared or received; for, altho' no
104 actual money might have passed, each company would have transferred the ownership of valuable property to one of its stockholders, who could thenceforth deal with it as he pleased, and could convert it into cash whenever he might desire. The fact that the stockholder happens to be incorporated can make no difference; the central question is, has a dividend been declared? If the Corporation has received a "dividend," this dividend has been declared by the Act to be "income," and, as income, Congress has directed it to be used in measuring both the taxes now in dispute. That the money (or property) handed over to the Corporation, was a dividend, we entertain no doubt. All the property transferred had been derived from earnings; none of it had become capital; it had been accumulated like cash, having been gained in the course of each subsidiary's business, and it awaited the pleasure of the respective boards of directors. These boards did not carry it to capital account; they did not issue stock to represent its value; they did not retain it for future use in their respective businesses; they decided to distribute it formally to their stockholders as a dividend, just as if it had been money; and they did in fact distribute it. No doubt one of the stockholders received almost all of it, but this did not change the character of the directors' act, which continued to be the declaration of a dividend, judged by the accepted tests; Gibbons v. Mahon, 136 U. S. 549. It can make no difference in the character of the directors' act, that the stockholder in question is a corporation and not an individual. Whether a distribution of corporate property is to be regarded as a dividend or not, does not depend on the status of the person that receives a share, but on what is done by the distributor. In the first instance the money or property is owned by the distributor, and as owner he has the power to decide what is to become of it. After the stockholder receives it, he may use it as he likes, but it comes into his hands as a dividend whether
105 he be an individual or a chartered company. We conclude therefore that the Gulf Oil Corporation received the property in question in the character of a separate stockholder in the subsidiaries, and received it as a dividend.

Being a dividend the Corporation received it after March 1, 1913, and the remaining question is, whether taxes have been laid upon it, and, if so, to what extent and in what manner? In thus speaking of a tax being laid upon property, we use the customary phrase; in strictness, taxes like the sum in question are not upon the property itself, but are exacted from the taxpayer because of his relation to the property. The owner pays, and the property measures the amount of the exaction. This is emphasized in the case before us, where two taxes are levied upon the same taxpayer; each tax is levied in respect of a different subject of taxation, but the amount of each is ascertained by the same measure, namely, by the taxpayer's income. For the year 1913, the Corporation was called upon to pay two taxes, one, an excise or a franchise tax for January and

February, and the other, an income tax for the remaining 10 months; but the amount of the excise tax was measured by the Corporation's income, and the amount of the tax in respect of the income itself was determined by the same measure. Before February 25, 1913, Congress could not tax the Corporation's income directly, but it could value its franchise according to its income, and could impose the tax on that basis: Maine vs. Railway Co., 142 U. S. 217. After the adoption of the Income Tax Amendment, Congress could tax the income directly, and for the remainder of the year it did tax the income in this manner. Each tax being computed by the same method, both were collected in one sum for convenience, but each depends for its validity on separate provisions. And we may add that Congress was not bound to go into a minute inquiry concerning the source of earnings that might be divided, or concerning the method by which they
106 had been accumulated. For we have to do with a situation where the property divided is concededly earnings, and our decision is confined to the facts before us.

The foregoing is the course of reasoning that commends itself to our minds, and we may briefly restate the conclusions. As levied by the Act of 1913, both taxes are constitutional, and each was distinctly laid on a separate subject of taxation. The excise or franchise tax was limited to the first two months of the year, and the value of the franchise was lawfully ascertained by using the Corporation's income as a measure; the income tax was for the remainder of the year, and was lawfully ascertained by using the same measure. In computing the Corporation's income the government lawfully took into account the valuable property over which the Corporation had acquired the complete ownership by virtue of its stock in the several subsidiaries, this ownership having been transferred to it by the formal declaration of a dividend. In exact terms the facts present the conditions laid down by the Act of Congress, and therefore (as no question is made concerning the regularity of the government's procedure) the amount of the two taxes was lawfully levied and collected.

The case of Lynch, Collector, vs. Turrish (C. C. A. 8) 236 Fed. 653, on which the Corporation relies with much confidence, does not seem to be in point. The facts were these; Turrish was a stockholder in the Payette Lumber Co. whose capital stock, $1,500,000 was invested in timber-lands. The Company did no business and earned no money, but the value of its lands increased gradually until on March 1, 1913, it had grown to be $3,000,000. In 1914 the Company sold the lands—that is, all its capital—for $3,000,000 and divided this sum among its stockholders. The share of Turrish was taxed as income received during 1914, and the court
107 of appeals decided that he was not liable—

"Because no income, gains, or profits, accrued to the plaintiff during the year 1914, or after March 1, 1913, but during that time his property remained of the same value, and because the sale of the property of the Payette Company in 1914 and the distribution of its proceeds by a dividend to its stockholders was but a change

of the form, without any increase of the value, of the property he owned before the Income Tax Law of 1913 took effect."

The case did not involve the question of an ordinary dividend from accumulated earnings, but decided that a sale of capital property and a distribution of the proceeds did not constitute the division of "income, gains, or profits" within the meaning of the Act of 1913. No such facts are before us now. We may add that the decision is to be reviewed by the supreme court.

A situation more like the case in hand is found in Southern Pacific Co. vs. Lowe (D. C.) 238 Fed. 847, where Judge Manton delivered an opinion that discusses the general subject satisfactorily. We shall not take up other citations in the briefs of counsel; most of them may be distinguished on their facts, and in any event the question here, if we have outlined it correctly, seems to suggest an answer that is reasonably plain. Moreover, the two cases just referred to cite and consider nearly all the cases to which our attention has been called.

One or two minor questions have been raised, but they do not require attention. The important points have been stated, briefly but we hope adequately, and if they have been correctly decided we see no need for a more elaborate discussion.

The judgment is reversed, with instructions to the district court to enter a judgment in favor of the collector.

Endorsed: No. 2254. Opinion of the Court by McPherson, J. Received & Filed October 8, 1917. Saunders Lewis, Jr., Clerk.

108 In the United States Circuit Court of Appeals for the Third Circuit, March Term, 1917.

No. 2254 (List No. 62).

C. C. LEWELLYN, Collector of Internal Revenue, Plaintiff in Error,

vs.

GULF OIL CORPORATION, Defendant in Error.

In Error to the District Court of the United States for the Western District of Pennsylvania.

This cause came on to be heard on the transcript of record from the District Court of the United States, for the Western District of Pennsylvania, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court, that the judgment of the said District Court in this cause be, and the same is hereby reversed, with instructions to the district court to enter a judgment in favor of the collector.

Philadelphia, October 8, 1917.

(Signed) JOHN B. McPHERSON,
Circuit Judge.

Endorsed: No. 2254. Order Reversing Judgment, etc. Received and filed Oct. 8, 1917. Saunders Lewis, Jr., Clerk.

109 UNITED STATES OF AMERICA,
Eastern District of Pennsylvania,
Third Judicial Circuit, set:

I, Saunders Lewis, Jr. Clerk of the United States Circuit Court of Appeals, for the Third Circuit, do hereby Certify the foregoing to be a true and faithful copy of the original transcript of record and proceedings in this Court in the case of C. C. Lewellyn, Collector of Internal Revenue, Plaintiff in Error, vs. Gulf Oil Corporation, Defendant in Error, No. 2254, on file, and now remaining among the records of the said Court, in my office.

In Testimony Whereof, I have hereunto subscribed my name and affixed the seal of the said Court, at Philadelphia, this first day of November in the year of our Lord one thousand nine hundred and seventeen and of the Independence of the United States the one hundred and forty-second.

[Seal of the United States Circuit Court of Appeals, Third Circuit.]

SAUNDERS LEWIS, JR.,
Clerk of the U. S. Circuit Court of Appeals, Third Circuit.

110 In the United States Circuit Court of Appeals for the Third Circuit, March Term, 1917.

No. 2254.

C. G. LEWELLYN, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, Plaintiff in Error,

vs.

GULF OIL CORPORATION, Defendant in Error.

Stipulation.

And now, January 21st, 1918, come Honorable John W. Davis, Solicitor General of the United States, representing C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, Plaintiff in Error, and James H. Beal and William Seifert, of counsel for the Gulf Oil Corporation, Defendant in Error, and stipulate and agree that the certified Transcript of Record on file in the Supreme Court of the United States in the case of Gulf Oil Corporation, Petitioner, vs. C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, at No. 781 October Term, 1917, shall be taken as the return to the Writ of

Certiorari granted by the Supreme Court of the United States in said case at said number and term.

JNO. W. DAVIS,
Solicitor General of the United States.
JAMES H. BEAL,
WILLIAM A. SEIFERT,
Of Counsel for Gulf Oil Corporation.

Endorsed: No. 2254. Stipulation. Received and Filed Jan. 24, 1918. Saunders Lewis, Jr., Clerk.

111 UNITED STATES OF AMERICA,
Eastern District of Pennsylvania,
Third Judicial Circuit, set:

I, Saunders Lewis, Jr., Clerk of the United States Circuit Court of Appeals, for the Third Circuit, do hereby Certify the foregoing to be a true and faithful copy of the original stipulation of counsel for return to writ of certiorari in the case of C. G. Lewellyn, Collector of Internal Revenue for the Twenty-Third District of Pennsylvania, Plaintiff in Error, vs. Gulf Oil Corporation, Defendant in Error, on file, and now remaining among the records of the said Court, in my office.

In Testimony Whereof, I have hereunto subscribed my name and affixed the seal of the said Court at Philadelphia, this twenty-fourth day of January in the year of our Lord one thousand nine hundred and eighteen and of the Independence of the United States the one hundred and forty-second.

[Seal of the United States Circuit Court of Appeals, Third Circuit.]

SAUNDERS LEWIS, JR.,
Clerk of the U. S. Circuit Court of Appeals, Third Circuit.

112 UNITED STATES OF AMERICA, *ss:*

[Seal of the Supreme Court of the United States.]

The President of the United States of America to the Honorable the Judges of the United States Circuit Court of Appeals for the Third Circuit, Greeting:

Being informed that there is now pending before you a suit in which C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, is plaintiff in error, and Gulf Oil Corporation is defendant in error, No. 2254, March Term, 1917, which suit was removed into the said Circuit Court of Appeals by virtue of a writ of error to the District Court of the United States for the Western District of Pennsylvania, and we, being willing for certain reasons that the said cause and the record and proceedings therein should be certified by the said Circuit Court of Appeals and

removed into the Supreme Court of the United States, do
113 hereby command you that you send without delay to the said supreme Court, as aforesaid, the record and proceedings in said cause, so that the said Supreme Court may act thereon as of right and according to law ought to be done.

Witness the Honorable Edward D. White, Chief Justice of the United States, the twelfth day of January, in the year of our Lord one thousand nine hundred and eighteen.

JAMES D. MAHER,
Clerk of the Supreme Court of the United States.

[Endorsed:] 2254. File No. 26,248. Supreme Court of the United States, October Term, 1917. No. 781. Gulf Oil Corporation vs. C. G. Lewellyn, Collector of Internal Revenue, etc. Writ of Certiorari. Received & Filed Jan. 21, 1918. Saunders Lewis, Jr., Clerk.

114 [Endorsed:] File No. 26,248. Supreme Court U. S., October Term, 1917. Term No. 781. Gulf Oil Corporation, petitioner, vs. C. G. Lewellyn, Collector of Internal Revenue, etc. Writ of certiorari and return. Filed January 25, 1918.

Office Supreme Court, U. S.
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JAMES D. MAHER,
CLERK

-14-

IN THE

Supreme Court of the United States

No. 7[redacted]310 OCTOBER TERM, 1917.

GULF OIL CORPORATION,
Petitioner,

vs.

C. G. LEWELLYN, Collector of Internal Revenue for the Twenty-third District of Pennsylvania,
Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit, and Brief in Support Thereof.

J. H. BEAL,
W. A. SEIFERT,
Attorneys for Petitioner.

REED, SMITH, SHAW & BEAL,
Of Counsel.

Smith Bros. Co. Inc., Franklin Print, 407-409 Grant Street, Pittsburgh, Pa.

INDEX.

	PAGE
Petition for Writ of Certiorari	1
Statement of the Matter Involved	2
Reasons for the Allowance of the Writ	7
Brief in Support of Petition	9
I. Special Reasons for granting the writ in the present case	9
II. The construction of the Income Tax Act of 1913	9
III. The Tax upon the full amount of the Dividends in Question cannot be sustained as a Franchise Tax	13
Paragraph S of Act of 1913	20

AUTHORITIES

Bailey vs. Railroad Co., 106 U. S., 109; 27 L. Ed. 81	8-11
Brushaber vs. Union Pacific R. R. Co., 240 U. S. 1	16
Collector vs. Hubbard, 79 U. S. 1	10
Gibbons vs. Mahon, 136 U. S. 549	10
Gould vs. Gould (not yet reported)	11
Lynch vs. Hornby, 236 Fed. 661	9
Lynch vs. Turrish, 236 Fed. 653	9

Hon. John W. Davis, Solicitor General:

You are hereby notified that the annexed Petition for Writ of *Certiorari* to the United States Circuit of Appeals for the Third Circuit in the case of C. G. Lewellyn, Collector of Internal Revenue for the Twenty-third District of Pennsylvania, vs. Gulf Oil Corporation, at No. 2254 March Term, 1917, will be presented to the Supreme Court of the United States on Monday, at the opening of Court on that day.

J. H. Beal

H. A. Lafferty

Attorneys for Petitioner.

And now, December ....., 1917, I accept service of the above notice and acknowledge to have received from Petitioner's counsel a copy of the Petition and Brief in this case.

.....

Attorney for Respondent.

IN THE

Supreme Court of the United States

No. **OCTOBER TERM, 1917.**

GULF OIL CORPORATION,
Petitioner,

vs.

C. G. LEWELLYN, Collector of Internal Revenue for the Twenty-third District of Pennsylvania,
Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit, and Brief in Support Thereof.

The Gulf Oil Corporation (a corporation of New Jersey) prays for a writ of *certiorari* to review the judgment of the Circuit Court of Appeals for the Third Circuit in the above entitled cause.

Statement of the Matter Involved.

This case involves the question of whether dividends aggregating $11,424,440.00, declared and payable by certain subsidiary companies to the Gulf Oil Corporation in January and February in 1913, out of surplus earnings of such companies accruing in the years 1907 to 1912, inclusive, such earnings having been used in the enlargement of the plants and properties of the companies in the conduct of their business (and upon which the Federal Excise Taxes had been paid), constitute taxable income to the Gulf Oil Corporation within the meaning of the Federal Income Tax Act of October 3, 1913.

The petitioner is a holding company organized in 1907. It carries on no business directly but through its subsidiary companies (all of the shares of which, except Directors' qualifying shares, being at all times owned by it); it carries on the business of producing and purchasing oil through producing companies in Oklahoma and Texas, transportation by pipe line companies in Oklahoma and Texas, and the refining and marketing of the manufactured products through the Refining Company with refineries at Port Arthur, Texas, which latter Company owns a fleet of steamships and various distributing stations and facilities.

No dividends from earnings were declared by the subsidiary companies from their organization until the declaration in January and February, 1913, of the divi-

dends in question, with the exception of some comparatively small dividends paid by three companies not material here. During this period, the earnings were large, but they were invested and re-invested and used in carrying on the various branches of the oil business, not necessarily that of the Company making the earnings, but all other subsidiaries of the parent Company.

Thus, all of the earnings of said Companies prior to December 31, 1912, were either invested as earned in the extension and development of the properties and business of the companies mentioned, or of the business of the several companies, and all were actually used and required in carrying on the business of the several subsidiary companies.

In January, 1913, the holding Company decided that the accumulated earnings and surplus of the subsidiary companies should be taken over on the books of the Gulf Oil Corporation and, accordingly, the dividends mentioned were declared. But as the surpluses and profits upon which the dividends were based did not consist of cash, but, on the contrary, of property and assets required for the conduct of the business of the Companies, the entire transaction was cleared upon the books of the holding Company and its subsidiaries, by a series of book entries, the result of which was to extinguish the existing indebtedness as *between* the subsidiary companies and to substitute for this an indebtedness *from* some of the subsidiaries to the Gulf Oil Corporation.

The manner in which the transaction was handled

is thus stated in its finding of fact, by the District Court and approved by the Court of Appeals, namely:

> "At the time of the declaration of the dividends before referred to all of the earnings of the subsidiary companies had been retained in those companies, treating the subsidiary companies collectively, although for the purposes of the enterprise as a whole it was necessary that the funds or credit of one subsidiary be loaned to and used by another. As a result of this at the time of the declaration of said dividends there existed among the subsidiary companies considerable indebtedness, evidenced by book accounts, such indebtedness arising almost entirely through transactions between such companies in the purchase and sale of oil or property."
>
> "All of these funds were either invested in properties or actually required in the carrying on of the business of the subsidiary companies, so that the subsidiary companies *were without moneys* with which to make payment of this inter-company indebtedness. For the purpose of clearing the transaction the matter was consummated on the same day, to wit: April 11, 1913, and in this way:
>
> The Gulf Oil Corporation took over upon its books the amount of the dividends before mentioned (other than the Indiana Oil and Gas Company and the Gulf Commissary Company, which it had already received) and at the same time set up upon its books accounts receivable owing to it by various subsidiaries aggregating the amount of the dividends so received. Upon the books of the subsidiary

companies entries showing the same facts were made, and all of these entries were made upon vouchers passed between the parties to the transactions.

As a result, the subsidiary companies collectively, after the payment of this dividend, owed substantially the same amount as prior thereto had been owing to some of the subsidiaries by other subsidiaries, but such indebtedness was shifted so that it was owing entirely to the Gulf Oil Corporation; and the Gulf Oil Corporation, after the payment of the dividends, had no property assets which prior thereto were not represented in the shares of stock of the subsidiary companies owned by it, but it had upon its books accounts receivable of subsidiary companies which together with the shares of stock of the various subsidiary companies owned by it represented the same property and assets as was represented by the shares of stock alone prior to the declaration and payment of said dividends."

The Collector assessed against the Gulf Oil Corporation a tax of one per centum upon the entire amount of these dividends under the Income Tax Act of 1913 and this tax the corporation paid under protest, took appropriate proceedings to enable it to sue and thereupon instituted the present suit in the District Court of the United States for the Western District of Pennsylvania, to recover $111,244.40, the amount of the taxes so paid. The case was tried by that Court without a jury and the facts as found are set forth in the opinion of the District Court (Record, page 70) and also in the

opinion of the Circuit Court of Appeals (Record, page 2 a).

The District Court entered judgment in favor of the plaintiff, holding that—

> "the dividends in question in this suit were not subject to the tax imposed because they were a distribution of surplus earnings arising through a period of years and which had accrued to and the equitable ownership thereof was vested in the plaintiff prior to January 1, 1913, and such earnings were not intended by Congress to be subject to taxation."

On appeal by the Collector, the Court of Appeals, in an opinion filed October 8, 1917, reversed the judgment of the District Court and held that the taxes were legally imposed.

Reasons for the Allowance of the Writ.

(1) The case is of great public importance, not only to the parties in this particular suit, but to all persons or corporations subject to the payment of Income Taxes under the legislation in question.

(2) There is a diversity in the decisions of the Courts as to whether such distributions are or are not taxable.

There are now pending in this Court the following cases involving similar questions, namely:

No. 421—*Lynch vs. Turrish;* and

No. 422—*Lynch vs. Hornby,* on writs of *certiorari* granted October 15th to the United States Circuit Court of Appeals for the 8th Circuit, that Court having held that such income is not taxable.

No. 452—*Southern Pacific Company vs. Lowe, Jr.,* on writ of error to United States District Court for the Southern District of New York.

No. 463—*Towne vs. Eisner, Collector,* on writ of error to the United States District Court for the Southern District of New York.

In both of the latter cases the District Court has held that such income *is* taxable.

The District Court for the Northern District of Illinois, Eastern Division, in *American Steel Foundries vs. Smietanka, Collector,* No. 32195, has recently held

(opinion not yet reported) that such income is *not* taxable and entered judgment against the Collector.

(3) The District Court in the present case held that it had a right to look to the character of the distribution made, and the fact that the earnings so distributed had all accrued prior to December 31st, 1912, and so viewing the case, held that such a distribution was not taxable income within the meaning of the act; while the Court of Appeals, disregarding the distinction, as between capital and income, and the character of the fund distributed, held that the case was to be determined solely upon the ascertainment of whether a dividend had been declared.

Such a rule would impose the tax upon a return of capital investment upon dissolution, if made by way of a dividend, and this manifestly was not the intent of Congress.

(4) The decision of the Court of Appeals confuses capital and income, and is contrary to the principles laid down by this Court in the construction and application of prior income tax laws, especially in *Bailey vs. Railroad Company,* 106 U. S., 109, 27 L. Ed., 81.

(5) The effect of the decision of the Court of Appeals is to make a different rule applicable to the dividends declared during the years 1913, 1914 and 1915 out of earnings accumulated prior to March 1, 1913, because prior to that date such dividends were not so taxable and by the subsequent legislation they are specifically excepted from being so taxed, whereas, all of the Income Tax Laws should as far as possible be so construed as to promote uniformity, especially as to what constitutes taxable income.

Brief in Support of Petition.

I. *Special Reasons for granting the writ in the present case.*

The special reasons already stated, especially the general importance of the questions involved and the diversity of the decisions in the courts thereon, brings this case within the class of cases in which this Court grants upon those grounds alone the writ of *certiorari*.

II. *The Construction of the Income Tax Act of* 1913:

The construction of the Act, as applied to earnings of the character distributed in the present case, is fully discussed by Judge Sanborn in the *Turrish case* (236 Fed., 653), and in the *Hornby case* (236 Fed., 661), and in the opinion of Judge Orr in the District Court in the present case. (See Record, page 70.)

The tax upon corporations is imposed by Paragraph G (a), and is upon the "net income arising or accruing" during the preceding calendar year; and the word "income" in the Act is used in connection with the words "gains and profits." It is only a dividend, which distributes a taxable gain or profit, that is within the Act, and surely the extraordinary distribution made here is not comprehended within such language.

Without attempting now to present our argument, we state briefly the following as our reasons for suggesting that the interpretation of the Act, as adopted by the Court of Appeals in the present case is erroneous:

(1) The Sixteenth Amendment, under which tne Act of 1913 was passed, authorizes the imposition of a tax without apportionment but the term "income" as therein used must be given its usual and ordinary meaning.

(2) Prior to the adoption of the amendment and of the passage of the Act of 1913, this Court held, in *Gibbons vs. Mahon*, 136 U. S., 549, as stated by the syllabus, as follows:

> "The interest in reserved or accumulated earnings of a corporation represented by each share is *capital*, and not income, on that share, as between the tenant for life and the remainderman thereof."

And, in *Collector vs. Hubbard*, 79 U. S., 1, this Court said:

> "a stockholder has no title for certain purposes to the earnings, net or otherwise, * * * prior to the dividend being declared,"

at the same time it held—

> "that the owner of a share of stock in a corporation holds the share with all its incidents, and that among those incidents is the right to receive all future dividends, that is, his proportional share ot all profits not then divided. * * * Regarded

as an incident to the shares, *undivided profits are property of the shareholder* and as such are the proper subject of sale, gift or devise."

(3) In *Bailey vs. Railroad Company,* 106 U. S., 109, this Court held, under the Income Tax Act of 1864, that the tax imposed by that Act upon dividends did not apply to the distribution by way of dividends of earnings accruing through a long period of years as to so much of the earnings so distributed as were accumulated in the years prior to the passage of the Act.

(4) In *Gould vs. Gould,* decided by this Court November 19, 1917, Mr. Justice McReynolds uses this language:

> "In the interpretation of statutes levying taxes, it is the established rule not to extend their provisions by implication beyond the clear import of the language used, or to enlarge their operations so as to embrace matters not specifically pointed out. In case of doubt they are construed most strongly against the Government and in favor of the citizen."

Keeping in mind then that the thing upon which the tax is authorized to be levied is *income*—that prior to the adoption of the amendment, this Court had held that reserved or accumulated earnings of a corporation were capital and not income, as between the tenant for life and the remainderman—that such undivided

profits were "an incident to the shares" and "*property* of the shareholder"—coupled with the fact that the Court had also held in the *Bailey case* that, under the Income Tax Act of 1864, the tax imposed by that act upon dividends did not extend to dividends made out of earnings accruing prior to the date at which the act became operative—we submit that Congress in 1913 must be deemed to have passed the present act in view of this settled law, and, clearly, that it does not *intend* to and did not intend to tax undistributed earnings accumulated through a period of years prior both to the passage of the act and to the adoption of the constitutional amendment.

This view of the Act is, we think, confirmed by the fact that the Income Tax Act of 1916 expressly limits all taxation thereunder, whether of dividends, of profits arising from sales, or otherwise, to income or profits accruing subsequent to March 1st, 1913, the date of the adoption of the constitutional amendment; and these limitations are again repeated in the War Revenue Act of 1917.

The Acts of 1913, 1916 and 1917 all relate to taxation of the same subject matter, and certainly, in the absence of a clear intent to the contrary, the construction of the entire legislation should be such as to produce uniformity of taxation thereunder. But, if the view of the Circuit Court of Appeals in the present case is to prevail, then we have two different rules applied to the taxation of the same subject matter, the difference being occasioned solely by the date of the distribution.

III. *The tax upon the full amount of the dividends in question cannot be sustained as a Franchise Tax.*

This question arises under Paragraph "S" of the Act of 1913 (36 Stat. at L., 201, chp. 16), which, for convenience, we print at length at the end of this brief.

That section provides that a special Excise Tax of one per centum upon corporations "for the period from January 1st to February 28th, 1913," be imposed, which tax shall be computed upon one-sixth of the entire net income of the corporation for the year—said net income to be ascertained in accordance with the provisions of said sub-section "G" of Section 2 of the Act of 1913.

Sub-section "G" referred to is the provision for the ascertainment of the *Income Tax* imposed upon corporations. The provisos then preserve the provisions of the Act of 1909 for the collection of the Excise Tax for the months of January and February, 1913, and further provide that it shall not be necessary to make more than one return and assessment for all taxes imposed upon corporations for the year 1913, either by way of income or excise. It further provides that:

> "The repeal of existing laws or modifications thereof shall not affect any act done or any right accruing or accrued * * * but all rights and liabilities under said law" (of 1909) "shall continue and may be in force in the same manner as if said repeal or modification had not been made."

(1) If the provisions of Paragraph "S" be so construed as to impose a different and more onerous Franchise Tax than imposed by the legislation in existence in January and February, then we have the serious question of the power of Congress to impose, by way of a Franchise Tax—a tax upon the privilege of doing business—different from that which existed at the time the privilege was exercised, and to impose such a tax after the privilege had been wholly exercised.

We submit that the Court will give such retroactive effect to a Franchise Tax only when imperatively required by the explicit language of the Act. The present Act is not only susceptible of, but properly bears quite a different construction, and one which avoids the constitutional question.

(2) The Franchise Tax, under the Act of 1913, is to be imposed only upon the *net income*, and this net income is to be ascertained in the same manner as *taxable net income* is ascertained under the prior provisions of the Act; so that it is clear that the proviso does not attempt to change or add to the *subject* of taxation. The thing to be taxed is still the taxable net income *accruing* to the corporation. True, the tax period is extended so as to continue the liability of the corporation to a Franchise Tax to the extent of one-sixth of its net income. But, unless the dividends in question are taxable as income, under the prior provisions of the Act, relating to the taxation of the net income accruing to corporations, then, clearly, they are

not taxable at one-sixth of their amount by way of a Franchise Tax under the proviso.

(3) *The Court will observe that in any event this would only effect the extent of our recovery for, as a Franchise Tax, the dividends would be subject to tax only to the extent of one-sixth thereof.*

However, if due effect is to be given to all of the provisions of the Income Tax Law of October 3, 1913—that is, if accrued rights and liabilities under the Excise Act of 1909 are to be preserved as if the repeal or modification had not been made—it can only be accomplished by assuming that Congress intended to subject such corporations to the Excise Tax as imposed by the Act of 1909 for the fraction of the year 1913, and we submit that such a construction of the Act is necessary to preserve its constitutionality. There would be no room to dispute this construction, were it not for the fact that the Act of 1913, while continuing the liability of corporations of the class described in Section 38 of the Act of 1909 to an Excise Tax, it provides, that the net income upon which the tax is to be measured shall be ascertained in accordance with the provisions of subsection "G" of the Act of 1913. These provisions differ from the method of ascertainment of the taxes as laid down in the Act of 1909, and we have this situation—that this Company having engaged in business on the 1st of January subject to the Excise Tax of 1909 and having transacted its business upon the faith of that legislation, on the 3rd of October, Congress undertook

to change its status and impose a different and a higher tax as a condition upon which the business already done should be transacted. An Excise Tax imposed upon the privilege of doing business necessarily operates *in futuro.* Doubtless Congress may at any time change terms or conditions, but after the business is done, we submit, it can not reach back and impose conditions different and more onerous and make the failure to comply with such *ex post facto* conditions punishable by fines and penalties.

Certainly we ought not to impute to Congress an intent which would render any part of the Act unconstitutional, but rather give to the Act that construction which makes effective and upholds every part thereof.

In *Brushaber vs. Union Pacific Railroad Company,* 240 U. S., 1, Mr. Justice White, in sustaining the validity of the Income Tax Act of 1913 against the objection that it was retroactive, used this language:

> "But the date of the retroactivity did not extend beyond the time when the amendment was operative."

Again, the Act of 1913 levied a tax on income, as such, and not upon capital. As was said in the *Brushaber case,* the tax on income under the Act of 1913 did not extend beyond the time when the amendment was operative. There could be, therefore, no tax upon income as such, under the Sixteenth Amendment dur-

ing the months of January and February, 1913. It will be observed that the dividends which passed to the Gulf Oil Corporation were declared out of earnings upon which Excise Taxes had been paid and which, after the taxes had been paid on them as such earnings, were put back into the plants of the subsidiary companies and were made to create additional earnings for the subsidiary companies, thus become capital, and as capital they were, as of December 31st, 1912, declared out by way of dividends to the Gulf Oil Corporation. The right of the Gulf Oil Corporation to have these dividends come to it without being subjected to an Income Tax was one of the rights which was continued and preserved under the proviso in paragraph "S" of the Act of 1913.

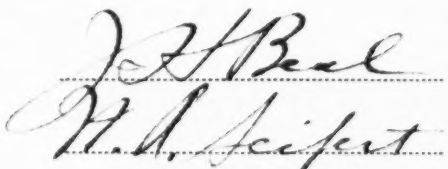
Summing up our suggestions upon this point we submit:

(1) That the Act did not intend to impose any other or different tax, by way of franchise, than the corporation would have been required to pay under the law as it existed at the time the privilege of doing business was exercised.

(2) That the Franchise Tax is to be imposed only upon taxable income, and, therefore, we come back to the question of whether these earnings constitute taxable income to the stockholder, regardless of whether it be a corporation or an individual.

(3) That such construction is the reasonable one, as it avoids imputing to Congress the intent of imposing arbitrarily a wholly different Franchise Tax from that which existed at the time the business was done, and also avoids any question of the constitutional power of Congress so to do.

We respectfully submit that the writ of *certiorari*, as prayed for, should be granted.



Attorneys for Petitioner.

REED, SMITH, SHAW & BEAL,
Of Counsel.

State of Pennsylvania, }
County of Allegheny, } ss:

W. J. Guthrie, being duly sworn, deposes and says that he is Secretary of the Gulf Oil Corporation, the Petitioner, and that the averments of fact contained in the foregoing petition are true and correct as he verily believes.

W. J. Guthrie

Sworn to and subscribed before me, this 7th day of December, 1917.

J. S. Dierker

Notary Public.

My commission expires Feby 21st 1919

PARAGRAPH S OF ACT OF 1913.

"S. * * * *Provided, further,* That all excise taxes upon corporations imposed by section thirty-eight, that have accrued or have been imposed for the year ending December thirty-first, nineteen hundred and twelve, shall be returned, assessed and collected in the same manner, and under the same provisions, liens and penalties, as if section thirty-eight continued in full force and effect: *And provided, further,* that a special excise tax with respect to the carrying on or doing of business, equivalent to 1 per centum upon their entire net income, shall be levied, assessed and collected upon corporations, joint stock companies or associations, and insurance companies, of the character described in section thirty-eight of the Act of August fifth, nineteen hundred and nine, for the period from January first to February twenty-eighth, nineteen hundred and thirteen, both dates inclusive, which said tax shall be computed upon one-sixth of the entire net income of said corporations, joint stock companies or associations, and insurance companies, for said year, said net income to be ascertained in accordance with the provisions of sub-section G of section two of this Act: *Provided further,* That the provisions of said section thirty-eight of the Act of August fifth, nineteen hundred and nine, relative to the collection of the tax therein imposed shall remain in force for the collection of the excise tax herein provided, but for the year nineteen

hundred and thirteen it shall not be necessary to make more than one return and assessment for all the taxes imposed herein upon said corporations, joint stock companies or associations, and insurance companies, either by way of income or excise, which return and assessment shall be made at the times and in the manner provided in this Act; but the repeal of existing laws or modifications thereof embraced in this Act shall not affect any act done, or any right accruing or accrued, or any suit or proceeding had or commenced in any civil case before the said repeal or modification; but all rights and liabilities under said laws shall continue and may be enforced in the same manner as if said repeal or modifications had not been made. * * *"

In the Supreme Court of the United States.

OCTOBER TERM, 1917.

GULF OIL CORPORATION, PETITIONER,
v.
C. G. LEWELLYN, COLLECTOR OF INTERNAL REVENUE, ETC.
No. 781.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

MOTION TO ADVANCE.

Comes now the Solicitor General, appearing on behalf of respondent, and moves to advance this case for hearing on a day convenient to the court.

The case presents the question whether dividends declared and payable by certain subsidiary corporations to the Gulf Oil Corporation in January and February, 1913, out of surplus earnings accruing to such subsidiary corporations during the years 1907 to 1912, inclusive, such earnings having been used in the enlargement of the plants and properties of the subsidiary companies in the conduct of their business (and upon which the Federal excise taxes had been paid), constitute taxable income to the Gulf Oil Corporation within the meaning of the Income-Tax Act of October 3, 1913.

41768—18

The case is of importance to the public revenues.

Notice of this motion has been served on opposing counsel.

JOHN W. DAVIS,
Solicitor General.

MARCH, 1918.

-16-

SEP 26 1918
JAMES D. MAHER,
CLERK.

IN THE

Supreme Court of the United States

310

No. [illegible] OCTOBER TERM, 1917.

GULF OIL CORPORATION,
Petitioner,

vs.

C. G. LEWELLYN, Collector of Internal Revenue for the Twenty-third District of Pennsylvania,
Respondent.

On a Writ of Certiorari from the United States Circuit Court of Appeals for the Third Circuit.

BRIEF FOR PETITIONER

J. H. BEAL,
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Attorneys for Petitioner.

REED, SMITH, SHAW & BEAL,
Of Counsel.

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INDEX.

	PAGE
STATEMENT OF THE CASE	1-5
SPECIFICATION OF ERRORS	6-7
POINTS OF LAW	8
BRIEF OF ARGUMENT	9-45

POINT I.

"Discussion of the recent Income Tax decisions in this Court"	9-21
Peabody vs. Eisner, U. S. Adv. Opinions, 1917-18, p. 650	9-10
Lynch vs. Turrish, U. S. Adv. Opinions, 1917-18, p. 639	10-12
Lynch vs. Hornby, U. S. Adv. Opinions, 1917-18, p. 646	12-16
Southern Pacific R. R. Co. vs. Lowe, U. S. Adv. Opinions, p. 643	16-21

POINT II.

"The surpluses which in form were distributed by the dividends in question consisted entirely of plants, properties and working assets, including cash working capital, and had been accumulated out of earnings through a period of years, all prior to January 1, 1913, and all thereof were essential and used in carrying on the oil business of petitioner and its subsidiaries; and, therefore, at the effectve date of the Act, these

surpluses constituted capital, and the so-called dividends were not subject to Income Tax under the Act of 1913" 21-28
Southern Pacific vs. Lowe, supra..... 26-27

POINT III.

"The dividends in question do not constitute taxable income, because they were dividends only in form, they resulted only in bookkeeping entries, with no gain or profit to petitioner, and the assets and property represented thereby had accrued to petitioner prior to January 1, 1913"..... 28-34
Southern Pacific vs. Lowe, supra..... 29
Gibbons vs. Mahon, 136 U. S., 549..... 29-30
Cook on Corporations, Vol. 2, 7th Ed., Sec. 554 30
Bailey vs. N. Y. C. & H. R. R. Co., 106 U. S., 109 30-32
Collector vs. Hubbard, 79 U. S., 1..... 33
Lynch vs. Turrish, supra..... 33-34

POINT IV.

"The dividends in question were not ordinary distributions to an ordinary stockholder, but were extraordinary, both in respect of the nature and character of the transaction and the recipient stockholder"..... 34-38
Lynch vs. Hornby, supra..... 36-38

POINT V.

"The special provisions of the Income Tax Act of 1913, regarding the tax on corporations for

the year 1913, do not subject the dividends in question to tax" 38-45
Income Tax Act of 1913 38-41
Brushaber vs. Union Pacific R. R. Co., 240 U. S., 1 43-44
Appendix (Excerpts from Income Tax Act of 1913) 46-49

CASES CITED.

Bailey vs. N. Y. C. & H. R. R. Co., 106 U. S., 109 30-32
Brainard, Collector vs. Hubbard, 79 U. S., 1 33
Brushaber vs. Union Pacific R. R., 240 U. S., 1 43-44
Gibbons vs. Mahon, 136 U. S., 549 29-30
Lynch vs. Hornby, U. S. Adv. Opinions, 1917,-18, p. 646 ..... 12-16, 36-38
Lynch vs. Turrish, U. S. Adv. Opinions, 1917-18, p. 639 ..... 10-12, 33-34
Peabody vs. Eisner, U. S. Adv. Opinions, 1917-18, p. 650 9-10
Southern Pac. R. R. vs. Lowe, U. S. Adv. Opinions, 1917-18, p. 643 ..... 16-21, 26-27, 29

OTHER AUTHORITIES.

Cook on Corporations, Vol. 2, 7th Ed., Sec. 554 30
Income Tax Act of 1913 38-41
(Clause "c" of Paragraph "G") 38-39
(Paragraph "S") 39-40

IN THE

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No. 781 OCTOBER TERM, 1917.

GULF OIL CORPORATION,
Petitioner,

vs.

C. G. LEWELLYN, Collector of Internal Revenue for the Twenty-third District of Pennsylvania,
Respondent.

On a Writ of Certiorari from the United States Circuit Court of Appeals for the Third Circuit.

STATEMENT OF THE CASE.

This case comes before the Court on a writ of *certiorari* issued to the Circuit Court of Appeals for the Third Circuit to review a judgment of that Court, reversing a judgment of the District Court.

The question involved is whether certain dividends aggregating $11,424,440, declared and payable to the petitioner Gulf Oil Corporation by its subsidiary companies in January and February, 1913, out of surplus accumulated by such subsidiary companies during the years 1907 to 1912 inclusive, constitute taxable income to the Gulf Oil Corporation within the meaning of the Federal Income Tax Act of October

3, 1913. The District Court held that they did not constitute such taxable income, while the Circuit Court of Appeals held that they did constitute taxable income.

The petitioner is a holding company, organized in February, 1907. It carries on no business directly, but through its subsidiary companies,—all of the shares of which, excepting directors' qualifying shares, were at all times owned by it,—it carries on the business of producing, transporting, refining and marketing oil and the products thereof.

From the organization of the holding company until the declaration in January and February, 1913, of the dividends in question, no dividends out of earnings were declared or paid by any of the companies in question, with the exception of some comparatively small dividends paid by three companies, not material here. During this period, the earnings were large, but they were invested and re-invested and used in carrying on the various branches of the oil business not necessarily that of the Company making the earnings, but other subsidiaries of the parent Company.

Thus, all of the earnings of said Companies prior to December 31, 1912, were either invested as earned in the extension and development of the properties and business of the companies mentioned, or of the business of the several companies, and all were then *actually used* and *required* in carrying on the business of the several subsidiary companies.

In January, 1913, the holding Company decided that the accumulated earnings and surpluses of the

subsidiary companies should be taken over on the books of the Gulf Oil Corporation and, accordingly, the dividends mentioned were declared. But as the surpluses and profits upon which the dividends were based did not consist of cash, but, on the contrary, of property and assets required for the conduct of the business of the Companies, the transaction was cleared upon the books of the holding Company and its subsidiaries, by a series of book entries, the result of which was to extinguish the existing indebtedness as *between* the subsidiary companies and to substitute for this an indebtedness *from* some of the subsidiaries to the Gulf Oil Corporation.

The manner in which the transaction was handled is thus stated in its finding of fact, by the District Court and approved by the Court of Appeals, namely (Record, pp. 38, 39):

> "At the time of the declaration of the dividends before referred to all of the earnings of the subsidiary companies had been retained in those companies, treating the subsidiary companies collectively, although for the purposes of the enterprise as a whole it was necessary that the funds or credit of one subsidiary be loaned to and used by another. As a result of this at the time of the declaration of said dividends there existed among the subsidiary companies considerable indebtedness, evidenced by book accounts, such indebtedness arising almost entirely through transactions between such companies in the purchase and sale of oil or property.
>
> "All of these funds were either invested in

properties or actually required in the carrying on of the business of the subsidiary companies, so that the subsidiary companies *were without moneys* with which to make payment of this inter-company indebtedness. For the purpose of clearing the transaction the matter was consummated on the same day, to wit: April 11, 1913, and in this way:

"The Gulf Oil Corporation took over upon its books the amount of the dividends before mentioned (other than the Indiana Oil and Gas Company and the Gulf Commissary Company, which it had already received) and at the same time set up upon its books accounts receivable owing to it by various subsidiaries aggregating the amount of the dividends so received. Upon the books of the subsidiary companies, entries showing the same facts were made, and all of these entries were made upon vouchers passed between the parties to the transactions.

"As a result, the subsidiary companies collectively, after the payment of this dividend, owed substantially the same amount as prior thereto had been owing to some of the subsidiaries by other subsidiaries, but such indebtedness was shifted so that it was owing entirely to the Gulf Oil Corporation; and the Gulf Oil Corporation, after the payment of the dividends, had no property assets which prior thereto were not represented in the shares of stock of the subsidiary companies owned by it, but it had upon its books accounts receivable of subsidiary companies which together with the

shares of stock of the various subsidiary companies owned by it represented the same property and assets as was represented by the shares of stock alone prior to the declaration and payment of said dividends."

The Collector assessed against the Gulf Oil Corporation a tax of one per centum upon the entire amount of these dividends under the Income Tax Act of 1913, and this tax the corporation paid under protest, took appropriate proceedings to enable it to sue and thereupon instituted the present suit in the District Court of the United States for the Western District of Pennsylvania, to recover $111,244.40, the amount of the taxes so paid. The case was tried by that Court without a jury and the facts as found are set forth in the opinion of the District Court (Record, pages 35-39), and also are adopted and set forth in the opinion of the Circuit Court of Appeals (Record, pages 49-57).

The District Court entered judgment in favor of petitioner. On appeal by the Collector, the Court of Appeals reversed the judgment of the District Court, and thereupon on application of the petitioner, this Court granted a writ of *certiorari*.

SPECIFICATION OF ERRORS.

1st. The Circuit Court of Appeals for the Third Circuit erred in entering the following order, which was entered October 8, 1917, viz:

> "This cause came on to be heard on the transcript of record from the District Court of the United States, for the Western District of Pennsylvania, and was argued by counsel.
>
> "On consideration whereof, it is now here ordered and adjudged by this Court, that the judgment of the said District Court in this cause be, and the same is hereby reversed, with instructions to the District Court to enter a judgment in favor of the collector."

2nd. The Court erred in holding that the dividends received by the petitioner from its subsidiaries constituted taxable income under the Income Tax Act of 1913.

3rd. The Circuit Court of Appeals erred in its opinion in stating and holding as follows (Record, pp. 54, 55):

> "Now, if the Corporation had been an individual, and had received the property in question by the method of transfer described in the findings of fact, the contention would hardly be made that no dividend had in fact been declared or received; for, although no actual money might have passed,

each company would have transferred the ownership of valuable property to one of its stockholders, who could thenceforth deal with it as he pleased, and could convert it into cash whenever he might desire. The fact that the stockholder happens to be incorporated can make no difference; the central question is, has a dividend been declared? If the Corporation has received a 'dividend,' this dividend has been declared by the Act to be 'income,' and, as income, Congress has directed it to be used in measuring both the taxes now in dispute. That the money (or property) handed over to the Corporation, was a dividend, we entertain no doubt. All the property transferred had been derived from earnings; none of it had become capital; it had been accumulated like cash, having been gained in the course of each subsidiary's business, and it awaited the pleasure of the respective boards of directors. These boards did not carry it to capital account; they did not issue stock to represent its value; they did not retain it for future use in their respective businesses; they decided to distribute it formally to their stockholders as a dividend, just as if it had been money; and they did in fact distribute it."

POINTS OF LAW.

I. Discussion of the recent Income Tax decisions in this Court.

II. The surpluses which in form were distributed by the dividends in question consisted entirely of plants, properties and working assets, including cash working capital, and had been accumulated out of earnings through a period of years, all prior to January 1, 1913, and all thereof were essential and used in carrying on the oil business of petitioner and its subsidiaries; and, therefore, at the effective date of the Act, these surpluses constituted capital, and the so-called dividends were not subject to Income Tax under the Act of 1913.

III. The dividends in question do not constitute taxable income, because they were dividends only in form, they resulted only in bookkeeping entries, with no gain or profit to petitioner, and the assets and property represented thereby had accrued to petitioner prior to January 1, 1913.

IV. The dividends in question were not ordinary distributions to an ordinary stockholder, but were extraordinary, both in respect of the nature and character of the transaction and the recipient stockholder.

V. The special provisions of the Income Tax Act of 1913, regarding the tax on corporations for the year 1913, do not subject the dividends in question to tax.

BRIEF OF ARGUMENT.

POINT I.

Discussion of Recent Income Tax Cases in This Court.

This Court has recently considered the construction to be placed upon the Income Tax Act of 1913, as regards the taxation of dividends, and for the purposes of the present case we do not deem it necessary to discuss the authorities further than to review these cases.

The cases to which we refer are the following: *Peabody vs. Eisner, Collector; Lynch vs. Turrish; Lynch vs. Hornby, and Southern Pacific R. R. Company vs. Lowe,* all decided June 3, 1918, and reported in Advance Opinions 1917-18, at pages 639 *et seq.*

The *Peabody case,* U. S. Adv. Opinions 1917-18, p. 650, involved the taxability of a dividend declared by the Union Pacific Railroad Company March 2, 1914, amounting to $3.00 in cash, $12.00 in par value of the preferred stock, and $22.50 par value of the common stock of the Baltimore & Ohio Railroad Company, which stock the Union Pacific Company had owned on and prior to March 1, 1913. The Court held the dividend taxable, saying that the case was controlled by the *Hornby case,* and in referring to the *Southern Pacific case,* the Court, by Mr. Justice Pitney, said (p. 651):

> *"Southern Pacific Co. vs. Lowe, Collector,* has been reversed, this day, *ante,* p. 643, 38 Sup. Ct. Rep., ..., but only upon the ground that the Central Pacific Railway Company,

which paid the dividend, and the Southern Pacific Company, which received it, were in substance identical corporations because of the complete ownership and control which the latter possessed over the former as stockholder and in other capacities, so that while the two companies were separate legal entities, yet in fact and for all practical purposes the former was but a part of the latter, acting merely as its agent and subject in all things to its direction and control; and for the further reason that the funds represented by the dividend were in the actual possession and control of the Southern Pacific Company as well before as after the declaration of the dividend. In this case the plaintiff in error stands in the position of the ordinary stockholder, whose interest in the accumulated earnings and surplus of the company are not the same before as after the declaration of a dividend; his right being merely to have the assets devoted to the proper business of the corporation and to receive from the current earnings or accumulated surplus such dividends as the directors in their discretion may declare; and without right or power on his part to control that discretion."

In the *Turrish case,* U. S. Adv. Opinions 1917-18, p. 639, Turrish was a stockholder in the Payette Lumber & Manufacturing Company, which company owned timber lands, but was not an operating company. Due to the gradual rise in the market value of the lands, the company's property was worth at March 1, 1913, substantially twice its par value, and about that time

Turrish and the other stockholders gave an option for the sale of their stock at twice its par value. Subsequently, the holder of the option, instead of exercising the same, proposed to purchase all of the assets of the Payette Company, which was done, the Payette Company, pusuant to resolutions of its stockholders and directors, conveying all its assets to a new company and receiving payment in cash of the purchase price, which it in turn distributed in dividends to its stockholders. In that case, this Court affirmed the decision of the District Court and of the Circuit Court of Appeals that no part of the amount so distributed to Turrish was income within the meaning of the Act of 1913, and this decision was rested upon two propositions expressed in the opinion of the Circuit Court of Appeals, by Sanborn, Circuit Judge, and approved by this Court in the opinion delivered by Mr. Justice McKenna, as follows (pp. 640-641):

> "The District Court and the Circuit Court of Appeals decided that the amount so distributed to Turrish was not income within the meaning of the statute, basing the decision on two propositions, as expressed in the opinion of the Circuit Court of Appeals, by Sanborn, Circuit Judge,—(a) The amount was the realization of an investment made some years before, representing its gradual increase during those years, and which reached its height before the effective date of the law, that is, before March 1, 1913, and the mere change of form of the property 'as from real to personal property, or from stock to cash' was not income to its holders because the value of the property was the same after as before the change; (b) The timber

lands were the property, capital and capital assets, of their legal and equitable owner and the enhancement of their value during a series of years 'prior to the effective date of an income tax law, although divided or distributed by dividend or otherwise subsequent to that date, does not become income gains, or profits taxable under such an act.'"

In the *Hornby case,* U. S. Adv. Opinions 1917-18, p. 646, Hornby was the owner of 434 out of 10,000 shares of the capital stock of the Cloquet Lumber Company, which company was engaged in purchasing timber lands, manufacturing of timber into lumber and selling it, and was so engaged in the year 1914, in which year it distributed dividends aggregating $650,000, and which it allotted or apportioned, $240,000 as being derived from current earnings, and $410,000 from conversion into money of property that it owned or in which it had an interest on March 1, 1913, and the question was whether Hornby's share of the latter amount was subject to income tax for the year 1914. The District Court and the Circuit Court of Appeals held that it was not so subject, but that decision was reversed by this Court and the case distinguished from the Turrish case, the opinion of the Court being delivered by Mr. Justice Pitney, in which at p. 648, he says:

"He (Hornby) was but one of many stockholders, and had but the ordinary stockholder's interest in the capital and surplus of the company, that is, a right to have them devoted to the proper business of the corporation and to receive from

the current earnings or accumulated surplus such dividends as the directors in their discretion might declare. *Gibbons vs. Mahon,* 136 U. S., 549, 557; 34 L. ed. 515, 526, 10 Sup. Ct. Rep., 1057. The operations of this company in the year 1914 were, according to the facts pleaded, of a nature essentially like those in which it had been engaged for more than a quarter of a century. The fact that they resulted in converting into money, and thus setting free for distribution as dividends, a part of its surplus assets accumulated prior to March 1, 1913, does not render Horbny's share of those dividends any the less a part of his income within the true intent and meaning of the Act."

Again, at page 648, Mr. Justice Pitney says:

"The Act took effect on March 1, 1913, a few days after the requisite number of States had given approval to the Sixteenth Amendment, under which for the first time Congress was empowered to tax income from property without apportioning the tax among the States according to population. *Southern Pacific Co. vs. Lowe, supra.* That the retroactivity of the Act from the date of its passage (October 3, 1913) to a date not prior to the adoption of the Amendment was permissible is settled by *Brushaber vs. Union Pacific R. R.,* 240 U. S., 1, 20; 60 L. ed. 493, 502; L. R. A., 1917 D, 414; 36 Sup. Ct. Rep,, 236; Ann. Cases 1917, B, 713. And we deem it equally clear that Congress was at liberty under the Amendment to tax as income, without apportionment, everything that became income, in the ordinary sense of the word,

after the adoption of the Amendment, including dividends received in the ordinary course by a stockholder from a corporation, even though they were extraordinary in amount and might appear upon analysis to be a mere realization in possession of an inchoate and contingent interest that the stockholder had in a surplus of corporate assets previously existing. Dividends are the appropriate fruit of stock ownership, are commonly reckoned as income, and are expended as such by the stockholder without regard to whether they are declared from the most recent earnings, or from a surplus accumulated from the earnings of the past, or are based upon the increased value of the property of the corporation. The stockholder is, in the ordinary case, a different entity from the corporation, and Congress was at liberty to treat the dividends as coming to him *ab extra,* and as constituting a part of his income when they came to hand.

"Hence we construe the provision of the Act that 'the net income of a taxable person shall include gains, profits, and income derived from * * * interest, rent, dividends, * * * or gains or profits and income derived from any source whatever' as including (for the purposes of the additional tax) all dividends declared and paid in the ordinary course of business by a corporation to its stockholders after the taking effect of the Act (March 1, 1913), whether from current earnings, or from the accumulated surplus made up of past earnings or increase in value of corporate assets,

notwithstanding it accrued to the corporation in whole or in part prior to March 1, 1913. In short, the word 'dividends' was employed in the Act as descriptive of one kind of gain to the individual stockholder; dividends being treated as the tangible and recurrent returns upon his stock, analogous to the interest and rent received upon other forms of invested capital."

And later in the opinion, at p. 650, the Court emphasizes the underlying thought as follows:

"We repeat that under the 1913 Act *dividends* declared and paid *in the ordinary course* by a corporation to its stockholders after March 1, 1913, whether from current earnings or from a surplus accumulated prior to that date, were taxable as income to the stockholder.

"We do not overlook the fact that every dividend distribution diminishes by just so much the assets of the corporation, and in a theoretical sense reduces the intrinsic value of the stock. But, at the same time, it demonstrates the capacity of the corporation to pay dividends, holds out a promise of further dividends in the future, and quite probably increases the market value of the shares. In our opinion, Congress laid hold of dividends paid *in the ordinary course* as *de facto* income of the stockholder, without regard to the ultimate effect upon the corporation resulting from their payment.

> "Of course we are dealing here with the *ordinary* stockholder receiving dividends declared *in the ordinary way of business. Lynch, Collector vs. Turrish* and *Southern Pacific Co. vs. Lowe, Collector,* this day decided, rest upon their special facts and are plainly distinguishable."

In the *Southern Pacific case,* U. S. Adv. Opinions 1917-18, p. 643, the question was whether certain dividends received by the Southern Pacific Company from the Central Pacific Railway Company in the early part of the year 1914, and claimed by the Southern Pacific Company to have been paid out of the surplus accumulated prior to March 1, 1913, were subject to income tax under the Act of 1913. It apeared that the Southern Pacific Company owned all of the stock of the Central Pacific Railway Company, which company owned a part of a large system of railways owned or controlled by the Southern Pacific Company. The Southern Pacific Company was in the actual physical possession of the railroads and other assets of the Central Pacific Company, in accordance with the terms of a lease under which the Southern Pacific Company was required to pay to the Central Pacific Company ten thousand dollars per annum for organization expenses and account annually for the net earnings in excess of six per cent. on the capital stock of the lessor company at the date of the lease. As a result of operations under the lease and of the conversion of certain capital assets of the Central Pacific Company, that company showed upon its books a large surplus accumulated prior to January 1, 1913, principally in the form of a debit against the Southern Pacific Company. The dividends in ques-

tion were declared and paid during the first six months of the year 1914, out of this surplus, the payment being carried into effect by bookkeeping entries, which simply reduced the apparent surplus of the Central Pacific and reduced the apparent indebtedness of the Southern Pacific to the Central Pacific by the amount of the dividends. This Court held that such dividends were not taxable and the opinion of the Court was delivered by Mr. Justice Pitney. After referring to the provisions of the Income Tax Act, he says (p. 644):

> "By Paragraph G (c), the tax upon corporations is to be computed upon the entire net income accrued within each calendar year, but for the year 1913, only upon the net income accrued from March 1 to December 31, to be ascertained by taking five-sixths of the entire net income for the calendar year.
>
> *"The purpose to refrain from taxing income that accrued prior to March 1, 1913, and to exclude from consideration in making the computation any income that accrued in a preceding calendar year, is made plain by the provision last referred to;* indeed, the Sixteenth Amendment, under which for the first time Congress was authorized to tax income from property without apportioning the tax among the States according to population, received the approval of the requisite number of States only in February, 1913. *Pollock vs. Farmers' Loan & Trust Co.,* 157 U. S., 429, 581; 39 L. ed. 759, 819, 15 Sup. Ct. Rep. 673; 158 U. S., 601, 637; 39 L. ed., 1108, 1125, 15 Sup. Ct. Rep., 912; *Brushaber vs. Union Pacific R. R.,* 240 U. S.,

1, 16; 60 L. ed. 493, 501, L. R. A. 1917 D, 414, 36 Sup. Ct. Rep. 236 Ann. Cas. 1917 B, 713.

"We must reject in this case, as we have rejected in cases arising under the Corporation Excise Tax Act of 1909 (*Doyle vs. Mitchell Brothers Co.*, ... U. S., ..., *ante*, 521, 38 Sup. Ct. Rep., ..., and *Hays vs. Gauley Mountain Coal Co.*,..... *U. S.*, ... *ante*, 525, 38 Sup. Ct. Rep., ..., decided May 20, 1918), the broad contention submitted in behalf of the Government that all receipts—everything that comes in—are income within the proper definition of the term 'gross income,' and that the entire proceeds of a conversion of capital assets, in whatever form and under whatever circumstances accomplished, should be treated as gross income. Certainly the term 'income' has no broader meaning in the 1913 Act than in that of 1909 (See *Stratton's Independence vs. Howbert*, 231 U. S., 399, 416, 417, 58 L. ed. 285, 293, 34 Sup. Ct. Rep., 136), and for the present purpose we assume there is no difference in its meaning as used in the two Acts. ***This being so, we are bound to consider accumulations that accrued to a corporation prior to January 1, 1913, as being capital, not income, for the purposes of the Act.*** And we perceive no adequate ground for a distinction, in this regard, between an accumulation of surplus earnings, and the increment due to an appreciation in value of the assets of the taxpayer.

"That the dividends in question were paid out of a surplus that accrued to the Central Pacific

prior to January 1, 1913, is undisputed; and we deem it to be equally clear that this surplus accrued to the Southern Pacific Company prior to that date, in every substantial sense pertinent to the present inquiry, and hence underwent nothing more than a change of form when the dividends were declared."

Again in the opinion (p. 645), it is said:

"We base our conclusion in the present case upon the view that it was the purpose and intent of Congress, while taxing 'the entire net income arising or accruing from all sources' during each year commencing the first day of March, 1913, *to refrain from taxing that which, in mere form only, bore the appearance of income accruing after that date, while in truth and in substance it accrued before;* and upon the fact that the Central Pacific and the Southern Pacific were in substance identical because of the complete ownership and control which the latter possessed over the former, as stockholder and in other capacities. While the two companies were separate legal entities, yet in fact, and for all practical purposes they were merged, the former being but a part of the latter, acting merely as its agent and subject in all things to its proper direction and control. And, besides, the funds represented by the dividends were in the actual possession and control of the Southern Pacific as well before as after the declaration of the dividends. The fact that the books were kept in accordance with the provisions of the lease, so that these funds appeared upon the

accounts as an indebtedness of the lessee to the lessor, cannot be controlling, in view of the practical identity between lessor and lessee. Aside from the interests of creditors and the public—and there is nothing to suggest that the interests of either were concerned in the disposition of the surplus of the Central Pacific—the Southern Pacific was entitled to dispose of the matter as it saw fit. There is no question of there being a surplus to warrant the dividends at the time they were made, hence any speculation as to what might have happened in case of financial reverses that did not occur is beside the mark.

"It is true that in ordinary cases the mere accumulation of an adequate surplus does not entitle a stockholder to dividends until the directors in their discretion declare them. *New York, etc., Railroad vs. Nickals,* 119 U. S., 296, 306, 30 L. ed. 363, 367, 7 Sup. Ct. Rep., 209; *Gibbons vs. Mahon,* 136 U. S., 549, 558, 34 L. ed. 525, 527, 10 Sup. Ct. Rep., 1057. And see *Humphreys vs. McKissock,* 140 U. S., 304, 312, 35 L. ed. 473, 475, 11 Sup. Ct. Rep., 779. But this is not the ordinary case. In fact the discretion of the directors was affirmatively exercised by declaring dividends out of the surplus that was accumulated prior to January 1, 1913; it does not appear that any other fair exercise of discretion was open; and the complete ownership and right of control of the Southern Pacific at all times material makes it a matter of indifference whether the vote was at one time or another. Under the circumstances, the entire matter of the declaration

and payment of the dividends was a paper transaction to bring the books into accord with the acknowledged rights of the Southern Pacific; and so far as the dividends represented the surplus of the Central Pacific that accumulated prior to January 1, 1913, they were not taxable as income of the Southern Pacific within the true intent and meaning of the Act of 1913."

POINT II.

The surpluses which in form were distributed by the dividends in question consisted entirely of plants, properties and working assets, including cash working capital, and had been accumulated out of earnings through a period of years, all prior to January 1, 1913, and all thereof were essential and used in carrying on the oil business of petitioner and its subsidiaries; and, therefore, at the effective date of the Act, these surpluses constituted capital, and the so-called dividends were not subject to Income Tax under the Act of 1913.

At the trial of the case before the District Court without a jury, certain facts were admitted, and as to others, testimony was taken, and findings of fact were made by the Court, the corectness of which is conceded. The material facts surrounding the making of the dividends in question and their payment are found in the 10th, 11th, 12th, 13th, 14th, 15th and 16th findings inclusive(Record, pages 37-39).

We summarize these findings and the testimony as follows: The petitioner is a holding corporation organized in February, 1907. It carries on no business directly, but through its subsidiary companies it carries on the business of producing and purchasing oil, through producing companies in Oklahoma and Texas,—the transportation by pipe line companies in Oklahoma and Texas of crude oil,—and the refining and marketing of the manufactured products through a refining company, with refineries at Port Arthur, Texas, which latter company owns a fleet of steamships and various distributing stations and marketing facilities.

The holding company owns no stocks outside of this particular enterprise (Record, page 26), and it owns all the shares of stock of its various subsidiary companies, with the exception of one share each to the qualifying directors (Record, page 29). The declaration of the dividends in question was made by five of the subsidiaries, namely, the J. M. Guffey Petroleum Company, $3,749,750; Gulf Pipe Line Company, $4,724,055; Gulf Pipe Line Company of Oklahoma, $2,597,660; the Indiana Oil and Gas Company, $338,000 and $10,000; and the Gulf Commissary Company, $4,975. All of these dividends were declared and payable in December, 1912, or in January and February, 1913, although the actual transaction of clearing or paying the dividends in some cases did not take place until April 11, 1913.

All of these dividends were declared out of accumulated surplus earned prior to January 1, 1913.

(See 11th, 12th, 13th, 14th and 15th findings of fact, Record pages 37-38.)

The transaction is thus described by the District Court in its 16th finding of fact (Record, pages 38 and 39):

> "Payment of said dividends by the J. M. Guffey Petroleum Company, the Gulf Pipe Line Company and the Gulf Pipe Line Company of Oklahoma, was made as follow:
>
> "The several companies mentioned, together with certain other companies, constituted a single enterprise carried on by the plaintiff, that enterprise consisting in a general way of the production and purchase of crude oil, the transportation of oil and the refining and marketing thereof. During the period in question the business of producing and purchasing oil was carried on principally in the State of Oklahoma, where also the oil was gathered and stored; the transportation of oil by pipe lines from points in the State of Oklahoma and in Texas to the Gulf of Mexico, where the company owned refineries in which the refined products were manufactured. The marketing of these products was carried on over a large part of the United States and in foreign countries, and for the purpose of shipping such refined products the Company owned and operated its own fleet of carrying vessels.
>
> "At the time of the declaration of the dividends before referred to all of the earnings of the subsidiary companies had been retained in those

companies, treating the subsidiary companies collectively, although for the purposes of the enterprise as a whole it was necessary that the funds or credit of one subsidiary be loaned to and used by another. As a result of this at the time of the declaration of said dividends there existed among the subsidiary companies considerable indebtedness, evidenced by book accounts, such indebtedness arising almost entirely through transactions between such companies in the purchase and sale of oil or property.

"All of these funds were either invested in properties or actually required in the carrying on of the business of the subsidiary companies, so that the subsidiary companies were without moneys with which to make payment of this intercompany indebtedness. For the purpose of clearing the transaction, the matter was consummated on the same day, to wit: April 11, 1913, and in this way:

"The Gulf Oil Corporation took over upon its books the amount of the dividends before mentioned (other than the Indiana Oil and Gas Company and the Gulf Commissary Company, which it had already received), and at the same time set up upon its books accounts receivable owing to it by various subsidiaries aggregating the amount of the dividends so received. Upon the books of the subsidiary companies entries showing the same facts were made, and all of these entries were made upon vouchers passed between the parties to the transactions.

"As a result, the subsidiary companies collectively, after the payment of this dividend, owed substantially the same amount as prior thereto had been owing to some of the subsidiaries by other subsidiaries, but such indebtedness was shifted so that it was owing entirely to the Gulf Oil Corporation; and the Gulf Oil Corporation, after the payment of the dividends, had no property assets which prior thereto was not represented in the shares of stock of the subsidiary companies owned by it, but it had upon its books accounts receivable of subsidiary companies which together with the shares of stock of the various subsidiary companies owned by it represented the same property and assets as was represented by the shares of stock alone prior to the declaration and payment of said dividends."

From these findings it is manifest that the entire transaction was a matter of form, the dividend declarations being the ordinary corporate action and the passing of vouchers, with the necessary memoranda for the making of the requisite bookkeeping entries to bring upon the books of the holding company evidence of the value of the shares of that company, as created by its ownership of all of the capital stock of the subsidiaries; and we have the distinct finding of fact by the Court that the transaction resulted in no gain or profit whatever to the holding company. Before the declaration and the bookkeeping entries, the holding company, through its ownership of the shares of the subsidiaries, owned all of the assets of those companies, whether capital or surpluses; after the declaration and the mak-

ing of the entries, the value of the holding company's ownership was precisely the same, but the form of it was changed, so that whereas prior to the transaction its ownership was entirely through the medium of the shares of stock of its subsidiaries; thereafter it was through the ownership of the shares of stock plus the accounts receivable owing by the subsidiaries to the holding company.

Observe further that the assets dealt with here are not mere accumulated earnings, but were in fact capital assets. Earnings may be accumulated in cash or investments, and if used independently of the company's business or not required in carrying on that business, they would retain their status of undistributed earnings. But when the earnings as made are put back into the business of the company, used to acquire new properties and facilities, which in turn create new earnings, and this continues for years, and at the end of the period we find all of the properties thus acquired and all of the earnings thus accumulated actually used and required,—as found by the Court in the present case,—in the conduct of the business of the company, surely such accumulations constitute capital, and when distributed by dividends, whether by an actual distribution, or, as in the present case, in form only, such dividends are not taxable income within the meaning of the Act.

The case is, therefore, we submit, directly within the decision of this Court in the *Southern Pacific case.* In that case, observing the provisions of a lease between the Southern Pacific and the Central Pacific, notwith-

standing the ownership of all of the shares of stock of the latter by the former, the bookkeeping and accounting had been conducted as though they were separate and distinct corporations, and under the terms of the lease a large debit balance was owing by the Southern Pacific to the Central Pacific. In this position the Central Pacific declared certain large dividends out of surplus accumulated prior to January 1, 1913, and payment was made regularly as though between parties at arms' length. However, of this transaction, this Court said (p. 644):

> "But the payment was only constructive, being carried into effect by bookkeeping entries, which simply reduced the apparent surplus of the Central Pacific and reduced the apparent indebtedness of the Southern Pacific to the Central Pacific by precisely the amount of the dividends."

And this Court held that such dividends were not taxable, summing up the result in these words (p. 645):

> "That the dividends in question were paid out of a surplus that accrued to the Central Pacific prior to January 1, 1913, is undisputed, and we deem it to be equally clear that this surplus accrued to the Southern Pacific Company prior to that date in every substantial sense pertinent to the present inquiry, and hence, underwent nothing more than a *change of form* when the dividends were declared."

Again, the Court will observe that in the present case, the surpluses to be dealt with were all invested

in property actually used in the conduct of the petitioner's business, through its various subsidiaries. They constitute definitely a part of the capital with which the enterprise was carried on. In this respect, the case differs from the *Peabody case,* where the shares of stock distributed, though owned prior to the effective date of the Act, yet were independent investments and were not a part of the capital reserved and used by the company in the conduct of its own business.

POINT III.

The dividends in question do not constitute taxable income because they were dividends only in form, they resulted only in bookkeeping entries, with no gain or profit to petitioner, and the assets and property represented thereby had accrued to petitioner prior to January 1, 1913.

We again call attention to the finding of fact made by the Court below in its 16th finding of fact (Record, pp. 38, 39), as follows:

> "The several companies mentioned, together with certain other companies, constituted a *single* enterprise *carried on by the plaintiff* (petitioner), that enterprise consisting in a general way of the production and purchase of crude oil, the transportation of oil and the refining and marketing thereof."

During the years 1907 to 1912, inclusive, all of the earnings of the petitioner's subsidiary companies had been reinvested in this "single enterprise carried on by the plaintiff,"—not necessarily in the company making the earnings, but either in that company or some other of the subsidiary companies. The result was that at the date of the dividend declarations, as found by the Court as a fact (Record, p. 38),

> "*All* of these funds were either invested in *properties* or *actually required* in the carrying on of the business of the subsidiary companies * * *."

The manner in which the dividend transaction was cleared by book entries has already been stated.

Under these circumstances, we submit to the Court that the earnings so reinvested in plants and properties from year to year constitute capital, and that all of such earnings accrued to and were represented by the shares of stock of the holding company,—the petitioner,—prior to January 1, 1913. *Southern Pacific Co. vs. Lowe,* already cited.

This rule logically results from the doctrine applicable in determining the rights as between a tenant for life and remainderman as respects a distribution of accumulated earnings.

In *Gibbons vs. Mahon,* 136 U. S., 549, this Court, in an opinion by Mr. Justice Gray, dealt very fully with that question, and the result is thus stated in the syllabus:

> "The interest in reserved or accumulated earnings of a corporation represented by each share is

capital, and not income, of that share, as between the tenant for life and the remainderman thereof."

The same doctrine is applied to extraordinary dividends paid from surplus accrued prior to the establishment of a trust, and the rule is referred to in *Cook on Corportaions* (Vol. 2, 7th Edition, Sec. 554), as the American Rule, thus:

> "This rule, inasmuch as it obtains in nearly every State in the Union, may well be called the American rule. It proceeds upon the theory that the Court, in disposing of stock or property dividends, as between life tenant and remainderman, may properly inquire as to the time when the fund out of which the extraordinary dividend is to be paid was earned or accumulated, and also as to the method of accumulation. If it is found to have accrued or been earned before the life estate arose, it may be held to be principal, and, without reference to the time when it is declared or made payable, to belong to the corpus of the estate, and not to go to the life tenant. But when it is found that the fund, out of which the dividend is paid, accrued or was earned, not before but after the life estate arose, then it may be held that the dividend is income, and belongs to the tenant for life."

The same doctrine was applied by this Court in *Bailey vs. New York Central & Hudson R. R. Company*, 106 U. S., 109. In that case the Government undertook to assess an Income Tax under the Act of 1864, upon a stock dividend made in 1868, distributing earnings accruing through the period from 1853 to 1868. The Court held that there was no authority for the imposi-

tion of the tax upon so much of the earnings as accrued prior to September, 1862, at which date the tax took effect. The tax in this case was assessed under an Act providing for a tax upon any dividend declared in scrip or money "payable to its stockholders as part of the earnings, profit, income or gains of such company, and all profits of such company carried to the account of any fund or used for construction," etc.

In the opinion (p. 113), Mr. Justice Matthews says:

> "These certificates were considered to be a dividend declared as of profits which had been, at some previous time, earned and converted into capital by an investment in permanent improvements of the railroad, and it was as representing such earnings that they were considered the subject of a tax. * * * It is now urged in argument by the counsel for the plaintiff in error (the Government), that, upon the express terms of this section, the certificates in question being a declaration of a dividend as part of the earnings, profits, income or gains of the Railroad Company, are taxable upon the amount theerof without deduction; that the policy as well as the language of the Act fixes the charge upon the declaration itself when made effectual as between the company and its stockholders, and, for the purposes of taxation, concludes both as the amount subject to the tax; * * * And, consequently, that when such a dividend has once been declared, and ascertained to come within the description of the law as a subject of taxation, all the rest follows, and the amount

declared is necessarily established as the amount to be taxed.

"The soundness of this mode of interpretation, and its application to ordinary cases, may well be admitted; but it cannot be applied to every case without a careful regard to its necessary limitations.

"It should be borne in mind, in the first place, that the tax provided for in this section of the Act, is an annual income tax, and its subject is the interest paid and profits earned by the company for each year, and year by year; and that both by the express letter of the law, and its necessary implications, the tax is not laid on any of these funds which came into being before the time prescribed in the Act. And in the ordinary execution of the law, it was contemplated, that the funds to be taxed and the tax imposed upon them, would be concurrent, as to each fiscal year; the scheme of the statute being to levy the tax upon the income for the year ending on the 31st of December next preceding the assessment; and, while it would be altogether admissible to go back, for the purpose of assessing a tax upon a proper fund which had accrued during a previous year and escaped taxation, nevertheless the tax imposed would be for the omitted year. But no tax, in contemplation of the law, accrues upon the fund, except for the year in which the fund itself accrued."

Again, in *Collector vs. Hubbard,* 79 U. S., 1, a tax case, this Court used the following language (p. 17):

> **"Decided cases are referred to, in which it is held that a stockholder has no title for certain purposes to the earnings, net or otherwise, of a railroad prior to the dividend being declared, and it cannot be doubted that those decisions are correct as applied to the respective subject-matters involved in the controversies. Grant all that, still it is true that the owner of a share of stock in a corporation holds the share with all its incidents, and that among those incidents is the right to receive all future dividends, that is, his proportional share of all profits not then divided. Profits are incident to the share to which the owner at once becomes entitled provided he remains a member of the corporation until a dividend is made. Regarded as an incident to the shares, undivided profits are property of the shareholder and as such are the proper subject of sale, gift or devise. Undivided profits invested in real estate, machinery, or raw material for the purpose of being manufactured are investments in which the stockholders are interested, and when such profits are actually appropriated to the payment of the debts of the corporation they serve to increase the market value of the shares, whether held by the original subscribers or by assignees."**

And in the recent case of *Lynch vs. Turrish,* this Court referred to the *Hubbard* case and the *Bailey case,* in the opinion Mr. Justice McKenna saying (p. 641):

"In *Collector vs. Hubbard, supra,* the distinction between a corporation and its stockholders was recognized and that the stockholder had no title for certain purposes to the earnings of the corporation, net or other, prior to a dividend being declared, but they might become capital by investment in permanent improvements and thereby increase the market value of the shares, 'whether held by the original subscribers or by assignees.' In other words, it was held that the investments of the corporation were the investments of the stockholders; that is, the stockholders could have an interest, taxable under the act considered, though not identical with the corporation. This was repeated in *Bailey vs. Railroad Company,* 22 Wall., 604, 635, 636."

Therefore, under the admitted facts of this case, we submit that the property and assets represented by the dividends in question constituted capital and accrued to the petitioner prior to the effective date of the Income Tax Act of 1913.

POINT IV.

The dividends in question were not ordinary distributions to an ordinary stockholder, but were extraordinary, both in respect of the nature and character of the transaction and the recipient stockholder.

The dividends in the present case represent the result of carrying on of petitioner's enterprise, through

its subsidiary companies, from 1907 to 1912, inclusive, and consist, not merely of the amount of the earnings, but of the property and assets created by the continual reinvestment of such earnings in the carrying on of the business. The result is that the surpluses of the various subsidiaries, represented by these dividends, were made up, not merely of earnings, but represented to that extent the value of the assets, including cash, of the various subsidiaries at January 1, 1913, which value had been created gradually through this period of years by the reinvestment of earnings. In other words, these surpluses were not a mere fund of money or personal property or investments arising from money earnings, but represented fixed properties and assets, including working capital, all used and actually necessary in the continued carrying on of petitioner's business.

Now, these surpluses might be brought upon the books of the holding company or reflected in its balance sheet in either one of two ways: (a) By the revaluation of the shares of stock of the subsidiary companies; or (b) by entries bringing upon the holding company's books the surpluses shown upon the books of the subsidiary companies. The latter method was adopted, and for that purpose the dividend declarations were made, but being merely the *form given to the transaction,* the petitioner ought not to be subjected to an income tax when it is found as a fact that no gain or profit whatever resulted to it.

We respectfully submit that dividends of this character paid to a holding company are not subject to tax,

and in support of this we refer to the *Hornby case.* The Court will remember that in that case the effort was to make an artificial distinction, whereby a part of the earnings of the Lumber Company would be allotted to its manufacturing operations, and the remainder thereof to the cutting and conversion of timber owned prior to the passage of the Act, upon the ground that this latter amount represented the difference between the value at March 1, 1913, of the timber so cut and manufactured and the cost of such timber. This Court refused to recognize this distinction, but in holding that the entire earnings of the company in 1914, to the extent declared in dividends were taxable, the opinion, by Mr. Justice Pitney, used this language (p. 649):

> "Hence, we construe the provision of the Act that 'the net income of a taxable person shall include gains, profits, and income derived from * * * interest, rent, dividends, * * * or gains or profits and income derived from any source whatever' as including (for the purposes of the additional tax) all dividends declared and paid in *the ordinary course of business* by a corporation to its stockholders after the taking effect of the Act (March 1, 1913), whether from current earnings, or from the accumulated surplus made up of past earnings or increase in value of corporate assets, notwithstanding it accrued to the corporation in whole or in part prior to March 1, 1913. In short, the word 'dividends' was employed in the Act as descriptive of one kind of gain to the individual stockholder; dividends being treated as the tan-

gible and *recurrent returns* upon his stocks, analogous to the interest and rent received upon other forms of invested capital."

And again, emphasizing the distinction sought to be made, at page 650, we find the following:

"In our opinion, Congress laid hold of dividends paid *in the ordinary course* as *de facto* income of the stockholder, without regard to the ultimate effect upon the corporation resulting from their payment.

Of course, we are dealing here with *the ordinary stockholder,* receiving dividends declared *in the ordinary way of business. Lynch, Collector, vs. Turrish,* and *Southern Pacific Company vs. Lowe, Collector,* this day decided, rest upon their special facts and are plainly distinguishable."

In other words, dividends *prima facie* constitute income; but, of course, it is necessary to look beyond the mere fact that the thing sought to be taxed is a dividend. A dividend may be a distribution of capital, and if so, it is not taxable. This right to investigate the character and nature of the transaction has been firmly asserted by this Court in the *Bailey case,* the *Southern Pacific case,* and the *Turrish case.* And it is upon this very point, as it seems to us, that the Circuit Court of Appeals erred; for the decision in that Court is put upon the ground that the Act taxed dividends, that what was received by petitioner came to it by way of a dividend declaration, and, therefore, fell

within the language of the Act. This Court, however, in the *Hornby case* has again asserted the right of the Court to examine the entire transactions, and so far as concerns distributions of earnings prior to March 1, 1913, they are taxable only where they are "dividends declared and paid *in the ordinary course* by a corporation to its stockholders,"—or, as again expressed, "where they are the tangible and *recurrent* returns upon other stock analogous to the interest and rent received upon other forms of invested capital,"—or, again, it must be the case of, "the *ordinary stockholder* receiving dividends declared *in the ordinary way of business.*"

POINT V.

The special provisions of the Income Tax Act of 1913, regarding the tax on corporations for the year 1913, do not subject the dividends in question to tax.

It is conceded, of course, that prior to the adoption of the Sixteenth Amendment, February 25, 1913, Congress was without power to levy the tax imposed by the Act of 1913 upon the income of corporations as well as individuals. Congress could, of course, and did, levy an Excise Tax upon corporations as the price of the privilege of doing business.

The Act of 1913, in respect of the tax upon corporations, provides [clause (c) of paragraph G]:

> "The tax herein imposed shall be computed upon its entire net income accrued within each preceding calendar year ending December thirty-first:

Provided, however, That for the year ending December thirty-first, nineteen hundred and thirteen, said tax shall be imposed upon its entire net income accrued within that portion of said year from March first to December thirty-first, both dates inclusive, to be ascertained by taking five-sixths of its entire net income for said calendar year."

And at the end of the Act (paragraph S) after repealing the Excise Tax of 1909, saving in pending cases, there is the following further proviso:

"And provided further, That a special excise tax with respect to the carrying on or doing of business, equivalent to 1 per centum upon their *entire net income,* shall be levied, assessed, and collected upon corporations, joint stock companies or associations, and insurance companies, of the character described in section thirty-eight of the Act of August fifth, nineteen hundred and nine, for the period from January first to February twenty-eighth, nineteen hundred and thirteen, both dates inclusive, which said tax shall be computed upon one-sixth of the entire net income of said corporations, joint stock companies or associations, and insurance companies, for said year, *said net income to be ascertained in accordance with the provisions of subsection G of section two of this Act*: Provided further, That the provisions of said section thirty-eight of the Act of August fifth, nineteen hundred and nine, relative to the collection of the tax therein imposed shall remain in force for the collection of the excise tax herein provided, *but for the year nineteen hundred and*

> ***thirteen it shall not be necessary to make more than one return and assessment for all the taxes imposed herein*** upon said corporations, joint stock companies or associations, and insurance companies, either by way of income or excise, which return and assessment shall be made at the times and in the manner provided in this Act; * * *."

Now, we submit that the fair and reasonable interpretation of the Act is that corporations should be liable for the income tax therein imposed for the ten months of the calendar year, March 1st to December 31st, and should be liable for the fraction of the Excise Tax imposed under the Act of 1909 for the two months, January and February. This is evidenced by the language of the Act of 1913, for observe it provides that the Act of 1909 shall be repealed only "except as hereinafter provided."

Also observe these further provisions:

> "that all excise taxes upon corporations imposed by Section Thirty-eight (the Act of 1909) that have accrued or have been imposed for the year ending December thirty-first, 1912, shall be returned, assessed and collected in the same manner and under the same provisions, liens and penalties as if Section Thirty-eight continued in full force and effect."

And that:

> "the provisions of said Section Thirty-eight of the Act of August fifth, 1909, relative to the collec-

tion of the taxes therein imposed, shall remain in force for the collection of the excise tax herein provided."

And that:

"the repeal of existing laws or modifications thereof embraced in this Act, shall not affect any act done or any right accruing or accrued, or any suit or proceeding had or judgment in any civil case before said repeal or modifications; but all rights and liabilities under said law shall continue and may be enforced in the same manner as if said repeal or modifications had not been made."

Observe that the provision regarding taxes for January and February comes by way of a proviso to the provisions repealing the Act of 1909.

The tax for January and February is to be computed upon "one-sixth of the entire net income * * * for said year," viz: the year 1913; and *"said net income* to be ascertained in accordance with the provisions of subsection "G" of Section 2 of this Act."

This proviso, therefore, does not attempt to change or add to the *subject* of taxation. What is to be taxed is still the net income accruing to the corporation. True, the tax period is extended so as to include the whole of the year 1913. But unless the dividends in question are taxable as income under the prior provisions of the Act relating to corporations then clearly they are not taxable under the proviso.

If due effect is to be given to all of the provisions of the Income Tax Law of October 3, 1913—that is, if accrued rights and liabilities under the Excise Act of 1909 are to be preserved as if the repeal or modification had not been made—it can only be accomplished by assuming that Congress intended to subject such corporations to the Excise Tax as imposed by the Act of 1909 for the fraction of the year 1913, and we submit that such a construction of the Act is necessary to preserve its constitutionality. There would be no room to dispute this proposition, were it not for the fact that the Act of 1913, while continuing the liability of corporations of the class described in Section 38 of the Act of 1909 to an Excise Tax provides, that the net income upon which the tax is to be measured shall be ascertained in accordance with the provisions of subsection "G" of the Act. This provision differs from the method of ascertainment of the taxes as laid down in the Act of 1909, and we have this situation—that this Company having engaged in business on the 1st of January subject to the Excise Tax of 1909 and having transacted its business upon the faith of that legislation, on the 3rd of October, Congress undertook to change its status and impose a different and a higher tax as a condition upon which the business already done should be transacted. An Excise Tax imposed upon the privilege of doing business necessarily operates *in futuro.* Doubtless Congress may at any time change terms or conditions, but after the business is done it may not reach back and impose conditions *ex post facto* and make the failure to comply with such *ex post facto* conditions punishable by fines and penalties.

Observe further that if such retroactive construction be given to this legislation the taxpayers are subject to the penalties provided in the Act; and thus a corporation would be subjected to the payment of an Excise Tax for the privilege of doing business already wholly completed and which had been so transacted under the faith of the legislation existing at that time, and made liable to penalties imposed after the transaction of the business in question. Such legislation would be clearly in violation of the constitutional provision against *ex post facto* legislation, and certainly we ought not to impute to Congress an intent which would render any part of the Act unconsitutional, but rather give to the Act that construction which makes effective and upholds every part thereof.

In the case of *Brushaber vs. Union Pacific Railroad Company,* 240 U. S., 1, 60 L. ed., 493, the Supreme Court, speaking through Chief Justice White, said:

> "The statute was enacted October 3, 1913, and provided for a general yearly income tax from December to December of each year. Exceptionally, however, it fixed a first period embracing only the time from March 1 to December 31, 1913, and this limited retroactivity is assailed as repugnant to the due process clause of the Fifth Amendment and as inconsistent with the Sixteenth Amendment itself. *But the date of the retroactivity did not extend beyond the time when the amendment was operative,* and there can be no dispute that there was power by virtue of the amendment during that period to levy the tax, without apportionment, and so far as

the limitations of the Constitution in other respects are concerned, the contention is not open, since in *Stockdale vs. Insurance Companies,* 20 Wall, 323, 331, in sustaining a provision in a prior income tax law which was assailed because of its retroactive character, it was said:

> 'The right of Congress to have imposed this tax by a new statute, although the measure of it was governed by the income of the past year, cannot be doubted; much less can it be doubted that it could impose such a tax on the income of the current year, though part of that year had elapsed when the statute was passed. The joint resolution of July 4, 1864, imposed a tax of five per cent. upon all income of the previous year, although one tax on it had already been paid, and no one doubted the validity of the tax or attempted to resist it.'"

It must be conceded that the Act of 1913 levied a tax on income, as such, and not upon capital. As was said in the *Brushaber case,* the tax on income under the Act of 1913 did not extend beyond the time when the amendment was operative. There could be, therefore, no tax upon income, as such, under the Sixteenth Constitutional Amendment during the months of January and February, 1913. It will be observed that the dividends which passed to the Gulf Oil Corporation were declared out of earnings upon which Excise Taxes had been paid and which, after the taxes had been paid on them as such earnings, were put back into the plants

of the subsidiary companies and were made to create additional earnings for the subsidiary companies, thus becoming capital, and as capital they were, as of December 31, 1912, declared out by way of dividends to the Gulf Oil Corporation. The right of the Gulf Oil Corporation to have these dividends come to it without being subjected to an Income Tax was one of the rights which was continued and preserved under the proviso in paragraph "S" of the Act of 1913.

We respectfully submit that the judgment of the Circuit Court of Appeals should be reversed and that of the District Court should be affirmed.

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APPENDIX.

EXCERPTS FROM INCOME TAX ACT OF 1913.

SECTION II..

A. Subdivision 1. "That there shall be levied, assessed, collected and paid annually upon the entire net income arising or accruing from all sources in the preceding calendar year to every citizen of the United States, whether residing at home or abroad, and to every person residing in the United States, though not a citizen thereof, a tax of 1 per centum per annum upon such income, except as hereinafter provided; and a like tax shall be assessed, levied, collected and paid annually upon the entire net income from all property owned and of every business, trade or profession carried on in the United States by persons residing elsewhere. * * *

B. "That, subject only to such exemptions and deductions as are hereinafter allowed, the net income of a taxable person shall include gains, profits and income derived from salaries, wages, or compensation for personal service of whatever kind and in whatever form paid, or from professions, vocations, businesses, trade, commerce, or sales or dealings in property, whether real or personal, growing out of the ownership or use of or interest in real or personal property, also from interest, rent, dividends, securities, or the transaction of any lawful business carried on for gain or profit, or gains or profits and income derived from

any source whatever, including the income from but not the value of property acquired by gift, bequest, devise or descent: Provided, that the proceeds of life insurance policies paid upon the death of the person insured or payments made by or credited to the insured, on life insurance, endowment, or annuity contracts, upon the return thereof to the insured at the maturity of the term mentioned in the contract, or upon surrender of the contract, shall not be included as income. * * *

G. (a) "That the normal tax hereinbefore imposed upon individuals likewise shall be levied, assessed, and paid annually upon the entire net income arising or accruing from all sources during the preceding calendar year to every corporation, joint-stock company or association, and every insurance company, organized in the United States, no matter how created or organized, but not including partnerships; but if organized, authorized, or existing under the laws of any foreign country, then upon the amount of net income accruing from business transacted and capital invested within the United States during such year. * * *

(c) "The tax herein imposed shall be computed upon its entire net income accruing during each preceding calendar year ending December thirty-first: *Provided, however,* that for the year ending December thirty-first, nineteen hundred and thirteen, said tax shall be imposed upon its entire net income accruing during that portion of said year from March first to December thirty-first, both dates inclusive, to be ascertained by taking five-sixths of its entire net income for said calendar year. * * *

8. * * * "*Provided, further,* That all excise taxes upon corporations imposed by section thirty-eight, that have accrued or have been imposed for the year ending December thirty-first, nineteen hundred and twelve, shall be returned, assessed and collected in the same manner, and under the same provisions, liens and penalties, as if section thirty-eight continued in full force and effect: *And provided, further,* that a special excise tax with respect to the carrying on or doing of business, equivalent to 1 per centum upon their entire net income, shall be levied, assessed and collected upon corporations, joint stock companies or associations and insurance companies, of the character described in section thirty-eight of the Act of August fifth, nineteen hundred and nine, for the period from January first to February twenty-eighth, nineteen hundred and thirteen, both dates inclusive, which said tax shall be computed upon one-sixth of the entire net income of said corporations, joint stock companies or associations, and insurance companies, for said year, said net income to be ascertained in accordance with the provisions of sub-section G of section two of this Act: *Provided, further,* That the provisions of said section thirty-eight of the Act of August fifth, nineteen hundred and nine, relative to the collection of the tax therein imposed shall remain in force for the collection of the excise tax herein provided, but for the year nineteen hundred and thirteen it shall not be necessary to make more than one return and assessment for all the taxes imposed herein upon said corporations, joint stock companies or associations, and insurance companies, either by way of income or excise, which return and assessment shall be made at the times and in the manner provided in this

Act; but the repeal of existing laws or modifications thereof embraced in this Act shall not affect any act done, or any right accruing or accrued, or any suit or proceeding had or commenced in any civil case before the said repeal or modification; but all rights and liabilities under said laws shall continue and may be enforced in the same manner as if said repeal or modifications had not been made. * * *"

INDEX.

	Page.
STATEMENT OF CASE	1–4
ARGUMENT	4–21
I. Burden of proof	4
II. The dividends were "income" within the meaning of the act of October 3, 1913	5
Meaning of Southern Pacific Company decision	5
Meaning of the decision in *Lynch* v. *Hornby*.	16
III. The validity of the corporation excise tax for the first two months of the year 1913	18
CONCLUSION	21

CASES CITED.

Anderson v. *Farmers' Loan and Trust Co.*, 241 Fed. 322	4
Brushaber v. *Union Pacific R. R. Co.*, 240 U. S. 1	20
Butterick Co. v. *United States*, 240 Fed. 539	20
Flint v. *Stone Tracy Co.*, 220 U. S. 107	21
Lynch v. *Hornby*, 247 U. S. 339	5, 8, 16
Lynch v. *Turrish*, 247 U. S. 221	17
Peabody v. *Eisner*, 247 U. S. 347	8, 17
Peterson v. *Chicago, R. I. & P. R. Co.*, 205 U. S. 364.	18
Pullman Palace Car Co. v. *Missouri P. R. Co.*, 115 U. S. 587	18
Southern Pacific Co. v. *Lowe*, 247 U. S. 330	5–8

In the Supreme Court of the United States.

OCTOBER TERM, 1918.

GULF OIL CORPORATION, PETITIONER,
v.
C. G. LEWELLYN, COLLECTOR OF Internal Revenue for the Twenty-third District of Pennsylvania. } No. 310.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF ON BEHALF OF LEWELLYN, COLLECTOR.

STATEMENT OF CASE.

This is an action to recover back taxes paid under protest, assessed under the provisions of the revenue act of October 3, 1913, 38 Stat. 114, 166, on the income of the Gulf Oil Corporation received by it during the year 1913.

The main question presented is whether certain dividends received by the Gulf Oil Corporation from other corporations were income within the meaning of the act. (R. 3–6; R. 17–30; R. 35–39.)

The Gulf Oil Corporation was a holding company and, as such, owned all the capital stock of the

J. M. Guffey Petroleum Company, the Gulf Pipe Line Company, the Gulf Pipe Line Company of Oklahoma, the Indiana Oil and Gas Company, and the Gulf Commissary Company, except the directors' qualifying shares (R. 19). The subsidiary corporations were engaged in the production, transportation, refining, and marketing of oil (R. 38), and the object of the holding company evidently was that the subsidiary companies, while carrying on their special businesses independently, should cooperate to the end of harmonious action from the beginning of the commercial process to its end (R. 21, 22). The Gulf Oil Corporation was a mere holding company. It had no tangible property except office furniture (R. 27), and "it does no business itself excepting the management of its interests as stockholder in these various companies" (R. 21). On the other hand, the subsidiaries had large plants and investments and were actively engaged in production, transportation, refining, and marketing of oil (R. 21, 22). It should be added that there were other companies subsidiary to the Gulf Oil Corporation than those whose dividends are involved in the case at bar (R. 26).

The subsidiary companies involved in this case had, prior to January 1, 1913, accumulated large surpluses (R. 20, 21, 24), part of which consisted of debts owing from other subsidiaries not involved in this suit (R. 24). Subsequent to January 1, 1913, the subsidiaries involved in this case declared and paid out of this accumulated surplus certain divi-

dends to their stockholders of record, including the Gulf Oil Corporation. These dividends were on their face paid in the usual way by vote of the board of directors and by checks duly drawn, delivered, and cashed (R. 20, 25). In fact, however, the dividends were apparently paid by a transfer of the obligations of the subsidiaries not involved in this case held by the dividend paying subsidiaries (R. 25, 26, 38, 39). Exactly how this was done can be best understood by taking a specific case which the witness was about to explain when interrupted by the court (R. 25). The Gulf Refining Company purchased its crude oil from the Gulf Pipe Line Company and as a result owed the Pipe Company a large sum of money. The Pipe Company, as payment of the aforesaid dividend, transferred this obligation to its stockholders. How the matter was arranged with the banks honoring the checks is not clear. The only explanation is that "they were cashed by the bank by offsetting accounts," although the checks were paid in the usual manner by giving credit for their face (R. 28). The money to pay them might have been borrowed from the bank on the bills receivable. The witness states that "the Gulf Oil Corporation practically advanced to the subsidiary companies the money necessary" (R. 28), but the Gulf Oil Corporation had no money to speak of (R. 27). If all parties used the same bank, as is probable, the bank might have given the Gulf Oil Corporation credit for the checks although there were no funds to pay them, and then might have

accepted the Gulf Oil Corporation's check to make them good *ex post facto*. At any rate, the burden of proof was on the plaintiff, and on this record it must be presumed that the dividends were regularly paid, either in cash, or in property equivalent to cash.

The District Court found the facts substantially (as far as it went) as above stated (R. 35–39), and held that the dividends so received were not income within the meaning of the act of October 3, 1913 (242 Fed. 709). The Court of Appeals reversed this decision, holding that the payments were true "dividends," and therefore income within the express language of the act (245 Fed. 1).

ARGUMENT.

I.

Burden of proof.

Since this is an action to recover taxes paid under an assessment made by the Commissioner of Internal Revenue under authority of law, and not an action by the United States to recover taxes not on the assessment roll, the burden of proof is upon the plaintiff, and it must establish by the preponderance of the evidence that the assessment was illegal. *Anderson* v. *Farmers' Loan and Trust Co.*, 241 Fed. 322, 329, and cases cited. Specifically as to the case at bar, the burden is on the plaintiff to show that the dividends in question were of such a character as to take them out of the ordinary class of dividends which are undoubtedly income.

II.

The dividends were "income" within the meaning of the act of October 3, 1913.

This question in its turn now depends simply upon the further question whether the case at bar is governed by the decision of this court in *Southern Pacific Co.* v. *Lowe*, 247 U. S. 330, or by its decision in *Lynch* v. *Hornby*, 247 U. S. 339.

Meaning of Southern Pacific Company decision.

In that case it appeared that the Southern Pacific Company owned all the capital stock of the Central Pacific Railway Company, including the stock registered in the names of the directors. The holding company operated a large system of railways, and in connection therewith was in the actual possession of the railroad and of other assets of the subsidiary, and in charge of its operations, pursuant to the terms of a lease which provided that the holding company should have possession of the railroads, branches, and leased lines belonging to the subsidiary, as part of its system, paying to the subsidiary $10,000 per annum for administration expenses and accounting annually for the net earnings. If these exceeded 6 per cent on the capital stock of the lessor, the lessee was permitted to retain for itself one-half of the excess. The Central Pacific Railway Company in 1914 declared and paid, by book adjustment with the holding company, which was acting as its banker, dividends out of the surplus which its books showed. It was held that these dividends were not taxable as income

of the holding company for 1914 under the Income Tax Act of October 3, 1913, because earned before March 1, 1913. The court was of the opinion (p. 335) that—

> * * * this surplus accrued to the Southern Pacific Company prior to that date, in every substantial sense pertinent to the present inquiry, and hence underwent nothing more than a change of form when the dividends were declared.

The court further said (p. 336):

> We do not rest this upon the view that for the purposes of the act of 1913 stockholders in the ordinary case have the same interest in the accumulated earnings of the company before as after the declaration of dividends;

and stated that its conclusion was based, in part (p. 337)—

> * * * upon the fact that the Central Pacific and the Southern Pacific were in substance identical because of the complete ownership and control which the latter possessed over the former, as stockholder and in other capacities. While the two companies were separate legal entities, yet in fact, and for all practical purposes they were merged, the former being but a part of the latter, acting merely as its agent and subject in all things to its proper direction and control. And, besides, the funds represented by the dividends were in the actual possession and control of the Southern Pacific as well before as after the declaration of the dividends. The fact that the books were kept in accordance with the provisions of the lease, so that these

funds appeared upon the accounts as an indebtedness of the lessee to the lessor, can not be controlling, in view of the practical identity between lessor and lessee.

The court also said (p. 338):

> It is true that in ordinary cases the mere accumulation of an adequate surplus does not entitle a stockholder to dividends until the directors in their discretion declare them. *New York, etc. Railroad* v. *Nickals*, 119 U. S. 296, 306; *Gibbons* v. *Mahon*, 136 U. S. 549, 558. And see *Humphreys* v. *McKissock*, 140 U. S. 304, 312. But this is not the ordinary case. In fact the discretion of the directors was affirmatively exercised by declaring dividends out of the surplus that was accumulated prior to January 1, 1913; it does not appear that any other fair exercise of discretion was open; and the complete ownership and right of control of the Southern Pacific at all times material makes it a matter of indifference whether the vote was at one time or another. Under the circumstances, the entire matter of the declaration and payment of the dividends was a paper transaction to bring the books into accord with the acknowledged rights of the Southern Pacific and so far as the dividends represented the surplus of the Central Pacific that accumulated prior to January 1, 1913, they were not taxable as income of the Southern Pacific within the true intent and meaning of the act of 1913.

To make sure that the case would not be taken as applying to ordinary holding companies and subsidiaries, the court three times, in three different cases, emphasized that the decision is limited to special facts.

In the opinion rendered in the case itself the court said (p. 338):

> The case turns upon its very peculiar facts, and is distinguishable from others in which the question of the identity of a controlling stockholder with his corporation has been raised.

In the case of *Lynch* v. *Hornby*, 247 U. S. 339, the court said (p. 346):

> * * * *Lynch* v. *Turrish* and *Southern Pacific Co.* v. *Lowe* rest upon their special facts and are plainly distinguishable.

In the case of *Peabody* v. *Eisner*, 247 U. S. 347, 349, the court said:

> * * * *Southern Pacific Co.* v. *Lowe* has been reversed this day, but only upon the ground that the Central Pacific Railway Co., which paid the dividend, and the Southern Pacific Co., which received it, were in substance identical corporations because of the complete ownership and control which the latter possessed over the former as stockholder and in other capacities, so that while the two companies were separate legal entities, yet in fact and for all practical purposes the former was but a part of the latter, acting merely as its agent and subject in all things to its direction and control; and for the further reason

> that the funds represented by the dividend were in the actual possession and control of the Southern Pacific Co. as well before as after the declaration of the dividend.

What, then, are the "very peculiar facts" referred to by the court as taking the *Southern Pacific Company* case out of the general rule?

1. *The lease.*—By a contract of lease between the subsidiary and the holding company, the former had divested itself of the custody of all its property, so that it had nothing which could be the basis of any dealings with any person except the holding company.

2. *The management.*—The court was not dealing with the case where a subsidiary's board of directors, though reflecting the policy of the controlling corporation, actually manages its business. The lease to the holding company left nothing to manage; everything was done by the holding company, not as agent, but in its own behalf.

3. *The source of money.*—It was not a case where the subsidiary collected money in a regular course of business dealings. The subsidiary was not a party to any contract with any person except its holding company, nor did the general public have any dealings with the subsidiary. The only source of income which the subsidiary had was the rent, graduated according to earnings, paid to it by the holding company.

4. *The character of dividends.*—The so-called dividend in favor of the holding company was only a book transaction; not only in the sense that the hold-

ing company made a practice of keeping the funds of the subsidiary, so that no money had to pass, but in a much broader sense; the subsidiary, since the time it had cut off all active business by executing the lease which divested it of its property, had collected no money from which this dividend could be declared. The holding company was in business for itself, utilizing the plant of the subsidiary as a part of its system. Money was received by the holding company in its own behalf, and remained the property of the holding company, except that at one time it was credited to the subsidiary's account and at another was charged against the subsidiary as dividends received from it.

Such a situation as existed between the Southern Pacific and the Central Pacific called for different treatment from the situation in which the subsidiary deals direct with the outside world in managing its property and affairs, and the rule applied to it can not be applied to the ordinary holding company.

All subsidiaries are necessarily in the control of the holding company; the ordinary and customary way of handling the money is for the holding company to be banker; the holding company can always control, through its representatives on the board, the time of declaring dividends. These are the normal and almost universal relationships between parent and subsidiary. If the court had intended to lay down a rule applicable to this common and general situation, is it conceivable that it would reiterate that the decision was based on special facts—the existence of the lease (which deprived

the subsidiary of any opportunity of separate action) and the fact that this corporation had never really earned or possessed the money (having no relations with the outside world)?

It seems clear that where the subsidiary really operates its property, making contracts with third persons in regular course of business, and either directly or through the holding company receiving payments and making disbursements as a party dealing with others than the holding company, this case does not apply.

The opinion makes the same distinction, in effect, which the Treasury Department has been making—between a subsidiary engaged in active business and one which has no business of its own and is little more than a name.

It is recognized by Article 208, Regulations No. 33 (Internal Revenue; revised), that in some cases the holding company makes all contracts and receives and disburses all the money in its own name, while the subsidiary is a mere shell, transacting no business with outsiders and having no actual source of income except mere book transactions between it and the holding company. That article reads:

> ART. 208. *Subsidiaries operated as integral parts.*—If subsidiary corporations exist in name only, or are mere agents or integral parts of the parent corporation and as such transact no business and have no income of and for their own account, and incur no expenses, all business being transacted, all income being

received and all expenses being paid directly by the parent company, no separate accounts being kept by or for such subsidiaries, it will be considered that such subsidiary concerns do not have any taxable income within the meaning of this title, and so long as they are so operated no tax liability will be asserted against them.

Subsidiaries to make returns.—In such cases, however, such subsidiary corporations will be required to make returns of annual net income, and shall indorse thereon a statement to the effect that the corporation making the return is a subsidiary or integral part of the parent company (naming it) and that, for its own account, it has no income from any source whatever, that it makes no disbursements, and that all the business done in its name is done for the account of and is the business of the parent corporation, and will be accounted for in the return of such parent corporation.

Southern Pacific Company v. *Lowe* involves a subsidiary of the same general class described in that article.

The department has been equally clear in ruling that active subsidiaries of the ordinary type are to be treated as entities distinct from the holding companies.

Thus, in Treasury Decision 2090, dated December 14, 1914 (16 Treas. Dec. Int. Rev. 259, 278), it is provided that every corporation, "no matter how closely related it may be to any other corporation, is required to make return of annual net income and to pay any income tax thereby

shown to be due." The fact that the parent or holding company owns all the stock of the subsidiary is immaterial and will not warrant such parent company in omitting or deducting dividends from such gross income. Treasury Decision 2137, dated January 30, 1915 (17 Treas. Dec. Int. Rev. 48, 59), provides as follows:

> *Returns of subsidiary companies—Where made.*—Under the provisions of the Federal income tax law and the regulations of this department, every corporation, joint-stock company or association, and every insurance company, regardless of its relation to another corporation, is held to be a separate and distinct entity, and unless it comes within the class of organizations specifically enumerated in the act as exempt must make a separate and distinct return, complete in every detail.

Article 207, Regulations No. 33 (revised), provides:

> If such branch corporation actually transacts business from which income arises, accrues, and is received by it, it will be incumbent upon such corporation to make a detailed return, as if it were in no way related to any other corporation, setting forth in such return the full amount of income which it receives or which accrues to it, together with the authorized deductions therefrom, and upon any net income thus disclosed the tax will be assessed and required to be paid.
>
> *Income of subsidiary paid to parent taxable as dividends.*—If the net income upon which

> the tax has been levied and is payable is turned over to the parent company, the holder of its stock, the amount so turned over will be held to be dividends, or amounts paid to it out of net earnings, and must be returned by the parent company for the purpose of the two per cent tax imposed by the act of September 8, 1916, but for the purpose of the war-income tax imposed by Title II of the act of October 3, 1917, the net income of the parent company may be reduced by the amount of dividends so received.

These rulings do not appear to be inconsistent with the opinion here considered.

Does the case at bar present the "very peculiar facts" on which the decision in *Southern Pacific Company* v. *Lowe* is said by the court to rest?

The statement of facts filed by the Gulf Oil Corporation in instituting its action does not contain any allegation, and apparently could not truthfully contain any allegation, that the holding company had custody of the plant of any of the subsidiaries, or that any contract or lease between the holding company and any subsidiary excluded the subsidiary from the possession or management of its plant, or cut it off from business dealings with persons other than the holding company, or that the holding company, rather than the officers and directors of each subsidiary, conducted the affairs of the subsidiary. Thus, Mr. Guthrie, the secretary of the plaintiff corporation, testifies that it does no business except look after its stock interests (R. 21, 26);

that the various subsidiaries actually carried on the activities for which they were organized; that the Gulf Refining Company (as an illustration of each subsidiary) had a considerable investment in plants and properties (R. 24); that the dividends were paid by check of the subsidiaries.

It thus appears that it is neither alleged nor proved that any one of the four vital features appearing in the case of *Southern Pacific* v. *Lowe* is present in the case at bar: (1) There was no contract by which a subsidiary gave up the power to manage its property; (2) the subsidiaries received money from and carried out contracts with the public generally, and were not limited to dealings with the holding company; (3) the officers and directors of each subsidiary managed its properties; (4) the funds from which the dividend was paid were received and earned by the individual subsidiaries in their dealings direct with their customers. The case presents merely the ordinary relationship between a holding company and its subsidiaries, without unusual or peculiar facts. The true condition of affairs is accurately summed up by the Court of Appeals as follows (245 Fed. 6):

> * * * We do not understand the Corporation to lay stress upon a supposed identity of the five subsidiaries with itself, but in any event the facts in proof would furnish a sufficient answer to such a position. No doubt all the companies are engaged together in a common enterprise, but the enterprise has

several branches, and each subsidiary attends to its own branch, while the Corporation does the like. Perhaps the Corporation may be more accurately described as uniting and regulating its subsidiaries; but each of the companies, whether holding or subsidiary, is a distinct entity, and is to be so treated. The several companies are not in such relations to each other that the property and obligations and liabilities of one can be regarded as the property and obligations and liabilities of any other. Each owns its own assets, carries on its own business, owes its own debts, pays its own taxes, and enjoys its own income. Under the Excise Act of 1909, each was separately taxed in respect of its own business, and under that act the Corporation certainly did not include in its own return the proceeds of the business done by the subsidiaries.

Meaning of the decision in Lynch v. Hornby.

The case of *Lynch* v. *Hornby, supra,* clearly decided that a dividend declared in the regular course of the operations of a corporation is not the less income under the act because it happens to be paid out of previously accumulated surplus. In that case there was no dispute that the amount in question was separately paid to Hornby as a division of capital assets. The conclusion of the court was, however, as follows (p. 346):

> We repeat that under the 1913 act dividends declared and paid in the ordinary course by a corporation to its stockholders after March 1, 1913, whether from current earnings or from a

surplus accumulated prior to that date, were taxable as income to the stockholder.

Clearly, therefore, the fact that in the case at bar the dividends were paid out of accumulated surplus is immaterial, as is also the fact, if it be a fact, that they were paid, not in money, but in bills receivable. *Peabody* v. *Eisner*, 247 U. S. 347. Moreover, they were paid in the ordinary course of business just as much as the dividends in the *Hornby* case. They were not winding up dividends, as in the case of *Lynch* v. *Turrish*, 247 U. S. 221. On the contrary, their payment did not disturb the regular business operations of the paying corporations, which continued after the payment in the same manner and to the same extent as before.

The only circumstance, therefore, disclosed by the present record to take the case out of the rule laid down in the *Hornby* case is the bare ownership by the Gulf Oil Corporation of practically all the stock of the dividend-paying corporations, with the concomitant power which stock ownership gives the stockholder.

In other words, the record does not disclose a single element making the relation of the Gulf Oil Corporation toward the dividend-paying corporation different from that of Hornby, except that it owned practically all of the stock in the paying corporation while Hornby only owned a portion. This, however, is not sufficient to differentiate the two cases for two reasons:

First, this court in the *Southern Pacific Company* case did not deem it sufficient, and consequently did

not rest its decision upon it, but upon the complete ownership and control which the Southern Pacific Company possessed over the railway company "as stockholder *and in other capacities*" (italics ours), and distinguished the case, therefore, from *Pullman Palace Car Co.* v. *Missouri P. R. Co.*, 115 U. S. 587, 596, and *Peterson* v. *Chicago, R. I. & P. R. Co.*, 205 U. S. 364, 391.

Second, the question whether a dividend paid in the regular course of business is income or not can not, on principle, be made to depend on the accident of the amount of stock held by the recipient of the dividend. If it could be, then the courts would be compelled to treat each case of the sort differently and to determine as to each one whether, *e. g.*, 100 per cent of the stock was necessary, or 90 per cent or 51 per cent, or even 30 per cent, if the latter amount was sufficient under the particular conditions to give control of the corporation. The distinction between the corporation and the stockholder is a fundamental one, and can not be disregarded unless the corporation is a mere agent, or instrumentality of the stockholder, as was held to be the fact in the *Southern Pacific Company* case.

III.

The validity of the corporation excise tax for the first two months of the year 1913.

The only other question raised in the petition is as to the validity of the corporation excise tax for the months of January and February, 1913. When

Congress came to enact the Income Tax Act of October 3, 1913, it was met with a doubt as to its power to tax incomes of individuals or corporations which had accrued prior to the passage of the Sixteenth Amendment. It was accordingly determined that as to the straight income tax only the last 10 months of 1913 should be taken. This, however, did not apply to the excise tax on the doing of business by corporations measured by their net income, and hence as to corporations Congress could lawfully cover the net income for the whole of the year 1913 by an excise on doing business for two months and by a straight income tax for the other ten. This might have been done by retaining the provisions of the act of August 5, 1909, for the first two months, but in that case it would have been necessary for corporations to make two returns for the year based on different principles, to the confusion and embarrassment of the taxpayer as much as the Government. Congress, therefore, adopted the method of levying a new excise on the doing of business for the months of January and February measured by one-sixth of the net income for the entire year, and a straight income tax on five-sixths of such income, the net income to be figured on the same basis for the whole year and only one return to be made. This it did by plain language in paragraph (c) of subsection G of Section II of the act (38 Stat. 174), and by subsection S of Section IV (38 Stat. 202), and it is impossible to construe these provisions (as the petitioner does), not as enacting

a new excise tax but as continuing the provisions of the old act of August 5, 1909, over the months of January and February, 1913.

It is equally impossible to construe the provisions of subsection S, *supra*, continuing the act of August 5, 1909, in force as to all excise taxes accrued during the year 1912, and saving rights accrued under the act of August 5, 1909, before its repeal, as extending that act over the months of January and February, 1913. To do so would be to contradict and nullify the positive provision of the subsection levying a new excise tax for the period from January 1 to February 28, and the words must therefore refer to taxes accruing prior to January 1 and to rights relative thereto. In addition to the decisions of the District Court and Court of Appeals in the present case approving this construction of the act, the same ruling was made by Judge Hand in *Butterick Co.* v. *United States*, 240 Fed. 539, 541.

As to the constitutionality of the act as so construed there can be no doubt, the point being in effect determined by *Brushaber* v. *Union Pacific R. R. Co.*, 240 U. S. 1, 20. If a past period going back to the time when an income tax could be constitutionally imposed was proper as to the straight income tax, the months of January and February could be separately taxed by an excise tax on doing business, according to the proportion they bore to the whole year, there being no constitutional obstacle to such a tax at that time. The petitioner had no vested right to continue doing business during Janu-

ary and February, subject only to the same tax imposed for the year 1912. If so, the same claim could be made as to its right to do business prior to the passage of the act of August 5, 1909, without paying any tax at all, and yet that act, which was sustained in *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, measured its initial levy by the net income for the whole of the year 1909.

CONCLUSION.

The judgment of the Circuit Court of Appeals should be affirmed.

W. C. HERRON,
Attorney.

OCTOBER, 1918.

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GULF OIL CORPORATION *v.* LEWELLYN, COLLECTOR OF INTERNAL REVENUE FOR THE TWENTY-THIRD DISTRICT OF PENNSYLVANIA.

CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

No. 310. Argued November 4, 1918.—Decided December 9, 1918.

Dividends of earnings by subsidiaries to a company holding all their stock and controlling them in conducting a single enterprise, the result of the transfers being merely that the main company became the holder of debts in the business, previously due from one subsidiary to another, *held* not taxable as income under the Income Tax Act of October 3, 1913, where the earnings were accumulated before the taxing year and had practically become capital. *Southern Pacific Co.* v. *Lowe*, 247 U. S. 330.
245 Fed. Rep. 1, reversed.

THE case is stated in the opinion.

Mr. Wm. A. Seifert, with whom *Mr. J. H. Beal* was on the brief, for petitioner.

Mr. William C. Herron for respondent.

MR. JUSTICE HOLMES delivered the opinion of the court.

This is a suit to recover a tax levied upon certain dividends as income, under the Act of October 3, 1913, c. 16, § II, 38 Stat. 114, 166. The District Court gave judgment for the plaintiff, 242 Fed. Rep. 709, but this judgment was reversed by the Circuit Court of Appeals. 245 Fed. Rep. 1. 158 C. C. A. 1.

The facts may be abridged from the findings below as follows. The petitioner was a holding company owning

all the stock in the other corporations concerned except the qualifying shares held by directors. These companies with others constituted a single enterprise, carried on by the petitioner, of producing, buying, transporting, refining and selling oil. The subsidiary companies had retained their earnings, although making some loans *inter se*, and all their funds were invested in properties or actually required to carry on the business, so that the debtor companies had no money available to pay their debts. In January, 1913, the petitioner decided to take over the previously accumulated earnings and surplus and did so in that year by votes of the companies that it controlled. But, disregarding the forms gone through, the result was merely that the petitioner became the holder of the debts previously due from one of its companies to another. It was no richer than before, but its property now was represented by stock in and debts due from its subsidiaries, whereas formerly it was represented by the stock alone, the change being effected by entries upon the respective companies' books. The earnings thus transferred had been accumulated and had been used as capital before the taxing year. *Lynch* v. *Turrish*, 247 U. S. 221, 228.

We are of opinion that the decision of the District Court was right. It is true that the petitioner and its subsidiaries were distinct beings in contemplation of law, but the facts that they were related as parts of one enterprise, all owned by the petitioner, that the debts were all enterprise debts due to members, and that the dividends represented earnings that had been made in former years and that practically had been converted into capital, unite to convince us that the transaction should be regarded as bookkeeping rather than as "dividends declared and paid in the ordinary course by a corporation." *Lynch* v. *Hornby*, 247 U. S. 339, 346. The petitioner did not itself do the business of its subsidiaries and have

possession of their property as in *Southern Pacific Co.* v. *Lowe*, 247 U. S. 330, but the principle of that case must be taken to cover this. By § II, G, (c), 38 Stat. 174, and S, *id.* 202, the tax from January 1 to February 28, 1913, is levied as a special excise tax, but in view of our decision that the dividends here concerned were not income it is unnecessary to discuss the further question that has been raised under the latter clause as to the effect of the fact that excise taxes upon the subsidiary corporations had been paid.

Judgment reversed.